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89-1620

No.

IN THE
Supreme Court of the United States
OCTOBER TERM, 1989

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., AND THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

Petitioners,

v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,

Respondent,

MERCHANTS NATIONAL CORPORATION,

Intervenor.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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April 18, 1990

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QUESTIONS PRESENTED*

1. Whether a reviewing court must apply a deferential standard of review to an administrative interpretation of a statute merely because the statutory language does not neatly answer the question presented to the court in a single sentence or paragraph.

2. Whether the nonbanking limitations of the Bank Holding Company Act, 12 U.S.C. § 1843, apply when a bank holding company engages in nonbanking activities through the direct ownership and operation of a state-chartered, subsidiary bank.

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* Pursuant to Rule 28.1, the petitioners state that the National Association of Professional Insurance Agents, only, has a parent company, subsidiary (other than wholly-owned), or affiliate. That subsidiary is Certified Professional Insurance Agent, Inc.

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OPINIONS BELOW

The decision of the court of appeals (Pet. App. A, pp. 1a to 19a, *infra*) is reported at 890 F.2d 1275 (2d Cir. 1989). The decision of the Board of Governors of the Federal Reserve System ("Board") (Pet. App. C, pp.

22a to 45a, *infra*) is reported at 75 Fed. Res. Bull. 388 (1989). The decision of the court of appeals in a related proceeding, *Independent Insurance Agents of America, Inc., et al. v. Board of Governors* is reported at 838 F.2d 627 (2d Cir. 1988) (Pet. App. E, pp. 47a to 63a, *infra*). The decision of the Board in a related proceeding is reported at 73 Fed. Res. Bull. 876 (1987) (Pet. App. G, pp. 67a to 82a, *infra*).

JURISDICTION

The decision of the court of appeals was issued on November 29, 1989. A timely motion for rehearing and suggestion for hearing in banc was denied on January 18, 1990 (Pet. App. D, p. 46a, *infra*). The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

Section 1841(b) and 1843(a) & (c)(8) of Title 12, United States Code, and 12 C.F.R. §§ 225.1(c)(3), 225.2 (d) & (l), and 225.21(a) are reproduced in Pet. App. H, pp. 83a to 90a, *infra*.

STATEMENT

This case will decide whether federally-regulated bank holding companies may avoid the severe constraints of the Bank Holding Company Act on their nonbanking activities simply by conducting those activities in state-chartered bank subsidiaries. That issue may sound arcane, but to the banking, insurance, real estate, and similarly-situated industries, it is a "long-simmering" and "major controversy in this country," App. A at 3a, that the Federal Reserve Board recognizes to be "important." [1] As one banking commentator remarked after the

[1] Opposition of Respondent Board of Governors of the Federal Reserve System to Petitioners' Motion for Stay of Mandate at 5, *Independent Insurance Agents of America, Inc., et al. v. Board of Governors*, No. 89-4030 (2d Cir.) (filed January 24, 1990). *See also* text at 8 *infra*.

appellate decision was rendered, "[f]rustrated . . . bank holding companies [can now] center [desired nonbanking] businesses in state-chartered affiliate banks." *Merchants National to Resume Sale of Insurance at Its Banks*, American Banker, Dec. 1, 1989 at 1.

Merchants National Corporation ("Merchants"), a bank holding company, is regulated by the Federal Reserve Board pursuant to the Bank Holding Company Act of 1956 ("BHCA" or "Act"), as amended, 12 U.S.C. § 1841, *et seq.* The Act offers a format by which ownership of banks and nonbanks can be combined within a single corporate structure, that is, a bank or nonbank company may acquire both banking and nonbanking subsidiaries so long as the parent holding company and those subsidiaries conform to the constraints of the BHCA.

In 1986, Merchants applied to acquire two state-chartered banks in Indiana; one was selling insurance directly through bank employees and the other, Mid State Bank, owned an insurance agency. Several of the petitioners objected on the ground that Merchants' ownership and operation of subsidiaries engaged in the sale of insurance would violate Section 4(c)(8) of the BHCA. That provision, in relevant part, states that bank holding companies may not "provide insurance as principal, agent, or broker."

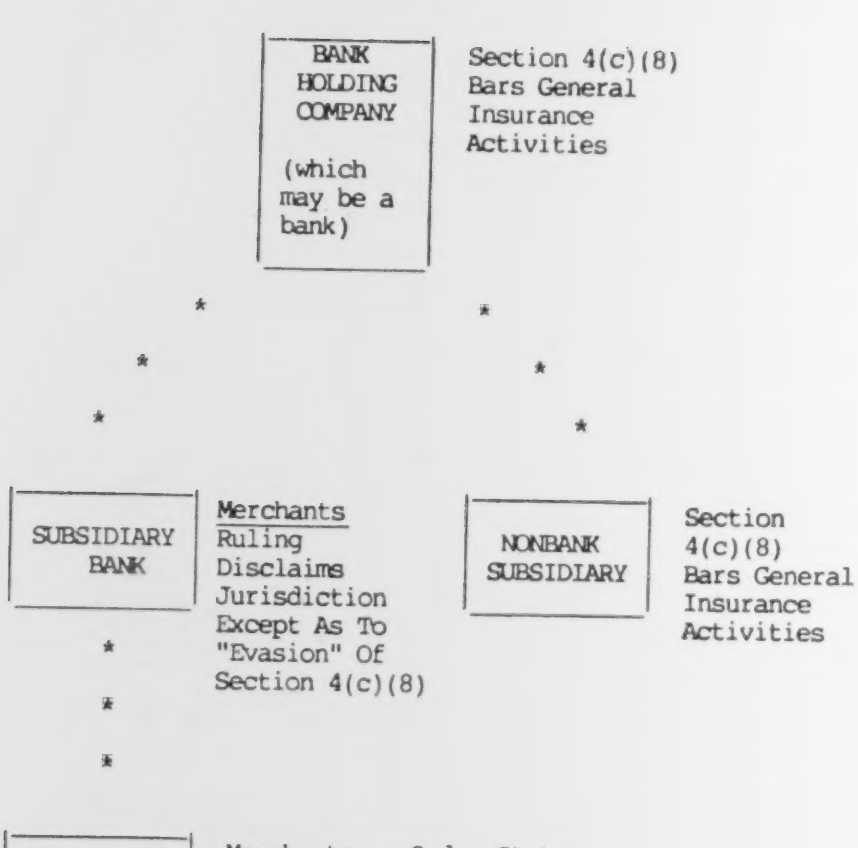
In 1989, the Federal Reserve Board approved Merchants' assumption of the insurance activities. *See Merchants National Corporation*, 75 Fed. Res. Bull. 388 (1989) (App. C at 22a) ("*Merchants* Order").[2] The

[2] Initially the Board had permitted Merchants to acquire the banks, but not their insurance activities. In 1987, the Board subsequently approved the acquisition of the insurance activities. *See Merchants National Corporation*, 73 Fed. Res. Bull. 876 (1987) (App. G at 67a). That order was reversed because its issuance violated a moratorium, then in effect, that prohibited the Federal Reserve Board from deciding this issue. *See Independent Insurance*

Board held that the nonbanking prohibitions of Section 4 generally do not apply to the direct activities of a subsidiary bank of a bank holding company. At the same time, the Board recognized that the insurance prohibition does apply if (i) the state bank is itself a bank holding company, (ii) the state bank subsidiary is being used to "evade" the purposes of the Act, or (iii) the state bank engages in insurance activities through its ownership of a separate nonbanking subsidiary. App. C at 28a, 41a. Thus, as the chart below depicts, the Board concluded that the nonbanking restrictions of Section 4(c)(8) are generally inapplicable so long as a bank holding company conducts its insurance activities inside a subsidiary bank, rather than through a nonbanking subsidiary. To thus avoid the application of Section 4(c)(8) to it, Merchants promised to dissolve the insurance agency owned by Mid State Bank and to move that business directly into the bank. App. C at 24a.

Prompt appellate review followed. *See* 12 U.S.C. § 1848. Over the Board's objection, the court granted a stay pending oral argument and, at oral argument, extended the stay pending decision. App. B at 20a, 21a.

Agents of America, Inc., et al. v. Board of Governors, 838 F.2d 627 (2d Cir. 1988) (App. E at 47a).



When it reached the merits, the court commented critically on the Board's interpretation of the scope of Section 4:

> Perhaps the most perplexing aspect of the structural arguments concerns the Board's contention that though it has no authority to preclude bank subsidiaries of a bank holding company from engaging in nonbank activities, it does have authority to preclude the subsidiaries of a bank subsidiary from engaging in nonbank activities. Thus, the Board adopts a generation-skipping approach: It may prohibit nonbank activities by bank holding companies and by their "grandchildren," *i.e.*, the subsidiaries of their bank subsidiaries, but not by their bank

"children," *i.e.*, the holding companies' immediate bank subsidiaries.

App. A at 14a. The court further found that the Board's interpretation (i) lacked "consistency," *id.* at 15a, (ii) failed to comport with the sole identified purpose behind the enactment of the insurance prohibition in Section 4(c)(8), *id.* at 15a, and (iii) afforded no explanation for plain language in the statute, *id.* at 14a. Nonetheless, the court believed that it must defer to the Board's "reasonable" interpretation because the express statutory language failed to state, in so many words, that conduct of the challenged activities in a subsidiary bank was subject to the insurance prohibition. App. A at 19a.[3]

REASONS FOR GRANTING THE WRIT

The ability of bank holding companies to enter nonbanking businesses free from the constraints of the BHCA has enormous practical and legal consequences.

Congress has separated the banking industry from general commercial activities in order to preserve the stability of banking institutions and to protect nonbanking businesses from the unfair effects of bank competition. The BHCA expressly focuses on the need to limit the nonbanking activities of holding companies, which can easily combine banking and nonbanking activities within a single corporate structure. But the ruling below enables bank holding companies to shrug off these constraints simply by conducting nonbanking activities directly within a subsidiary bank rather than through a nonbanking subsidiary of the holding company. Such intracorporate maneuvering exposes the commercial banking industry to the same morass that has befallen the savings & loan industry, whose excesses will cost American tax-

[3] The Second Circuit subsequently denied a petition for rehearing and a suggestion for hearing in banc. App. D at 46a. An Application for a Stay of Mandate of the U.S. Court of Appeals for the Second Circuit was denied by Justice Stevens on February 2, 1990.

payers billions of dollars. The entry of bank holding companies into nonbanking businesses ruled off-limits by Congress also threatens bank consumers—potential victims of credit coercion—and competing industries—put in competition with banking entities able to use the federal safety net and federal deposit insurance for their narrow competitive advantage.

These unprecedented, nationwide consequences flow from the Second Circuit's fundamental misreading of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The court, in common with other courts, failed to understand that no deference is due to an administrative interpretation until after a court fully analyzes congressional intent using all of the "traditional tools of statutory construction." *Id.* at 843 n.9. Rather, the court adopted a deferential standard of review immediately upon concluding that the express statutory language does not neatly answer the question presented to it.

Correct application of *Chevron* requires that the *Merchants* Order be struck down as inconsistent with the language and purpose of the BHCA. The insurance prohibition provides generally that it is not permissible for "a bank holding company to provide insurance as a principal, agent or broker," Section 4(c)(8), 12 U.S.C. § 1843(c)(8); a prohibition that is designed to "implement a congressional policy against control of banking and nonbanking enterprises by a single business entity.'" App. A at 10a (quoting *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980)). Accordingly, the statute's insurance bar applies to every insurance activity in which a bank holding company may engage.

The lower courts' systematic abrogation of *Chevron*'s careful two-step analysis inevitably leads courts to accord unwarranted deference to administrative interpretation—a result that inevitably shifts power from Congress, whose intent has not been fully explored, to administrative

agencies, which have the later word. In an era of divided government particularly, that misuse of *Chevron* erodes basic principles of shared power among the branches of the federal government.

I. THE ABILITY OF BANK HOLDING COMPANIES TO ENTER NONBANKING BUSINESSES FREE FROM THE RESTRAINTS OF THE BANK HOLDING COMPANY ACT RAISES IMPORTANT, NATIONAL ISSUES THAT SHOULD BE RESOLVED BY THIS COURT

The *Merchants* Order holds that the BHCA does not generally limit the nonbanking activities of bank holding companies so long as the bank holding companies conduct those activities directly through a state-chartered subsidiary bank. As even the Board acknowledges, that issue raises "significant legal questions" involving "important and fundamental legal and policy issues." *Board Statement on Applications to Acquire State-chartered Banks in South Dakota at* 1, 2 (Jan. 5, 1984). Indeed, the court below recognized that the *Merchants* Order contravenes the basic purpose of the BHCA: " 'to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity.' " App. A at 10a (quoting *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980)); *id.* at 15a.

The *Merchants* Order threatens immediate and nationwide consequences. Congress intended the nonbanking limitations of the Act to protect the financial stability of the nation's banking system, S. Rep. No. 1095, 84th Cong., 1st Sess. 5 (1955), and to ensure that banking institutions cannot (i) abuse their role as impartial arbiters of credit, (ii) tie the provision of banking services, like loans, to the sale of nonbanking products, like insurance, and (iii) assume an unfair advantage over nonbanking competitors by virtue of their unique access to federally-insured funds. H.R. Rep. No. 609, 84th Cong., 1st Sess. 16 (1955); 115 Cong. Rec. 32894 (1969) (Chairman

Patman). In fact, the Board itself recently explained that the BHCA limits the ability of subsidiary banks to operate nonbanking businesses in order to ensure that (i) the risks of commercial activities are not underwritten by federal deposit insurance funds, and (ii) commercial competition is not distorted. 53 Fed. Reg. 48915, 48918 (Dec. 5, 1988).[4]

Without the application of the BHCA to all parts of a holding company system, the spread of nonbanking powers for bank holding companies will go far "beyond the academic or the episodic." *Rice v. Sioux City Memorial Park Cemetary, Inc.*, 349 U.S. 70, 74 (1955). A professional association of state bank regulators has concluded that a number of states are now in the business of granting nonbanking authority to their state-chartered banks that exceed the limits of the BHCA:

Insurance Underwriting (5 States)
Insurance Brokerage (12 States)
Real Estate Equity Participation (23 States)
Real Estate Development (23 States)
Real Estate Brokerage (6 States)
Securities Underwriting (17 States)
Securities Brokerage (21 States).[5]

State willingness to authorize nonbanking activities includes, in addition, the operation of an amusement park,

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[4] Consistent with these policies, the Board has ruled courier services off-limits to the subsidiary banks of bank holding companies, 12 C.F.R. § 225.129 (1973); 38 Fed. Reg. 32126 (Nov. 21, 1973), and this Court has affirmed the Board's power to restrict the manner in which bank subsidiary employees can be involved in the permissible activities of a securities affiliate. *See Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981); 12 C.F.R. § 225.125(h) (1989).

[5] Statement of James Gilleran on behalf of The Conference of State Bank Supervisors Before The House Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the Committee on Banking, Finance and Urban Affairs of the House of Representatives, Attachment 2 (April 4, 1990).

see Federal Reserve Board Docket No. R-0652 (comments of New Jersey Bankers Ass'n) (letter of Jan. 27, 1989), and, in the thrift context, the ownership of windmill farms. *See Money Brokers Deserve Share of Blame For Thrift Woes*, American Banker, March 3, 1989 at 5. The Delaware State Senate is now considering a bill, passed by the House, designed to grant Citicorp and other large, money center bank holding companies the power to underwrite and sell insurance nationwide. *Insurers, Lawmakers Raise Concerns About Implications of Merchants National Ruling*, Banking Report (BNA) No. 14, at 611 (April 9, 1990).

The ability of bank holding companies to enter risky businesses directly threatens to compromise the financial stability of bank holding companies. One cause of the current S&L crisis was state willingness to permit their state-chartered institutions to engage in a wide variety of nonbanking activities, including, most notably, real estate investment. *See New Estimate on Savings Bailout Says Cost Could Be $500 Billion*, The New York Times, April 7, 1990 at A1. The cost of resolving the S&L mess has escalated sharply; it is now estimated at one half a trillion dollars. *Id.* The risk to bank holding companies from real estate development and property & casualty insurance underwriting, to name but two examples, is too plain to be doubted. *See also* 52 Fed. Reg. 543, 544 (Jan. 7, 1987) (Board statement that real estate investment activity involves a "significant degree of risk").

Apart even from risk to their own stability, "there is little question that bank holding companies can and do provide the rawest form of unfair competition for small businessmen."[6] Consumers of commercial services and products will face the fear and threat of banks tying the

[6] Bank Holding Company Legislation and Related Issues: Hearings on H.R. 2255, H.R. 2427, H.R. 2856, H.R. 4004 Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban

availability of credit to the purchase of commercial products. Similarly, commercial competitors will confront (i) the loss of customers subjected to coercion or simply unwilling to risk the loss of their bank's credit, (ii) the loss of credit if they compete with banks that are both creditor and competitor, and (iii) the competitive disadvantage created by their bank competitors' access to cheap funds brought into the bank as a result of federal deposit insurance.

These concerns are not speculative. In 1969, the House Banking Committee heard testimony "concerning the kind of pressure banks have exerted to gain customers for various departments of the bank," and Congress was told "how banks can use their life and death power to grant or withhold credit to influence critical policy decisions of nonbanking corporations." 115 Cong. Rec. 32894 (1969) (statement of Chairman Patman). Within the past three weeks, the insurance commissioner of a state that permits insurance sales by its state-chartered banks told Congress that he personally has been subjected to bank coercion, despite federal and state anti-tying laws. J. Long, Testimony Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs (April 4, 1990).

The danger inherent in implementation of the Board Order is so patent that the Second Circuit twice stayed that order over the Board's objections. Large bank holding companies have taken advantage of the ruling to conduct activities declared impermissible by the Act. Just this month, for example, the nation's ninth largest bank holding company announced plans to sell insurance in 77 bank offices in California by the end of 1990. That action follows on the heels of "aggressive" insurance sales efforts already conducted in California by the nation's fifth

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Affairs, 96th Cong., 1st Sess. 2 (1979) (remarks of Cong. St Germain).

largest bank holding company. *See First Interstate Targets Insurance*, American Banker, April 11, 1990 at 6; *Top 100 U.S. Bank Holding Companies*, American Banker, April 11, 1990 at 10, 12. Before the dangers threatened by the *Merchants* Order can come to full fruition, this Court should consider whether Congress intended these results.

II. THE SECOND CIRCUIT, IN COMMON WITH OTHER FEDERAL COURTS, FAILED TO APPRECIATE AND APPLY THE IMPORTANT PRINCIPLES OF *CHEVRON U.S.A., INC. v. NATURAL RESOURCES DEFENSE COUNCIL, INC.*

In *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), this Court enunciated the fundamental standards to guide judicial review of administrative decisions. *First*, a court must use "traditional tools of statutory construction," to determine "whether Congress has directly spoken to the precise question at issue." *Id.* at 842, 843 n.9. *Second*, and if "the statute is silent or ambiguous with respect to the specific issue," the court must determine whether the administrative agency has rendered a "permissible construction of the statute." *Id.* at 843; *see Sullivan v. Everhart*, 110 S.Ct. 960 (1990).

Each step has its own independent significance in ensuring the separation of powers. The first step ensures that original congressional intent receives the greatest deference and that close examination of legislative materials, including most obviously the language of the statute itself, precedes any attempt to ascertain how administrative agencies currently view the meaning or purpose of the law. Failure to follow legislative intent carefully would "usurp a power which our democracy has lodged in its elected legislature." F. Frankfurter, *Some Reflections on the Reading of Statutes*, 47 Col. L. Rev. 527, 534 (1947). The requirement that congressional intent be

carefully observed and fully vindicated is especially important in an era of divided government, when an administrative agency may be governed by appointees of one political party, and one or both of the houses of Congress controlled by another. Our federal system of government was designed, after all, to provide "a vigorous Legislative Branch and a separate and wholly independent Executive Branch . . . ." *Bowsher v. Synar*, 478 U.S. 714, 722 (1986).

Unfortunately, a number of courts, including the court below, have focused on step two to the detriment of step one. To be sure, an apt understanding of the judicial role mandates that courts not trench upon the legitimate function of an administrative agency. Disregard of the importance of step one, however, devalues the importance of congressional intent and subordinates the role of the legislative branch. Yet many courts, including the court below, believe that their authority under step one permits only a glancing look at the statute for a sentence that straightforwardly answers the question presented to the court by the litigants. But cases that easy seldom require the attention of the federal courts, and the federal courts, when they are called upon to decide issues of statutory interpretation, are "not to assay whether Congress might have stated that intent more naturally, more artfully, or more pithily." *Sullivan v. Everhart*, 110 S.Ct. at 973 (Stevens, J., dissenting).

The court below began and ended its independent review of congressional intent with the observation "We find no provision that says, in substance, 'The Board may not regulate the activities of bank subsidiaries of bank holding companies [or that says] 'Bank subsidiaries of bank holding companies may not engage in nonbank activities.'" App. A at 11a-12a. Without study of the express statutory language and congressional purpose, *id.*, the court then moved hastily to step two and pronounced the Board interpretation "permissible." That

failure to apply *Chevron* correctly proved to be outcome determinative. *See* Part III *infra*.

The court's error reflects a wide-spread difficulty in the lower courts. For example, in *Verna v. Coler*, 893 F.2d 1238 (11th Cir. 1990), the court adopted a *Chevron* analysis that, "[r]ather than beginning the analysis by determining whether Congress has clearly expressed its intent . . . proceeds to the second question and considers whether the agency's interpretation of the statute is reasonable." *Id.* at 1240 (Hatchett, J., dissenting). *See also Lile v. University of Iowa Hospitals and Clinics*, 886 F.2d 157, 160 (8th Cir. 1989) (deferring to an agency immediately upon finding that a statutory term, "governmental program," was ambiguous).

That problem has affected a number of other cases involving the Board. In *National Association of Casualty & Surety Agents v. Board of Governors*, 856 F.2d 282 (D.C. Cir. 1988), *reh'g en banc denied*, 862 F.2d 351, *cert. denied*, 109 S.Ct. 2430 (1989), even plain language was insufficient to prevent the court from analyzing the agency action under step two. In that case, the court asserted without explanation that an express statutory term "might be thought to be a fortuitous choice . . .", and went on to uphold an administrative interpretation even though the court "prefer[ed] petitioners' construction of the statute over the Board's." *Id.* at 288, 289; *see id.* at 291-92 (Buckley, J., dissenting) (the "language could hardly be more precise. . . . If a statute is unambiguous, as it is in this case, judicial inquiry is normally complete").[7] Similarly, in *Securities Industry Ass'n*

[7] In a concurrence to the appellate court's denial of rehearing en banc, the circuit judges representing the majority view explained, without modifying their earlier opinion, that they found the relevant statutory provision ambiguous, but continued to assert that "a myopic focus on Congress' selection of a definite or indefinite article could occasion results that . . . would be unexpected." *National Association of Casualty & Surety Agents v. Board of Governors*, 862 F.2d 351, 353 (D.C. Cir. 1988).

v. Board of Governors, 807 F.2d 1052, 1056 (D.C. Cir. 1986), the court moved to step two before examining the statute or other indicia of congressional intent. In order to safeguard principles of the separation of powers, this consistent misunderstanding of *Chevron* requires this Court's immediate attention.

III. THE NONBANKING LIMITATIONS OF THE BANK HOLDING COMPANY ACT APPLY TO ALL SUBSIDIARIES OF A BANK HOLDING COMPANY

The second issue raised by this petition is, of course, whether the *Merchants* Order comports with the requirements of the BHCA, which generally states that it is not permissible "for a bank holding company to provide insurance as a principal, agent, or broker . . . ." Section 4(c)(8), 12 U.S.C. § 1843(c)(8). For three basic reasons, the *Merchants* Order cannot survive close analysis.

First, the clear language of Section 4(a)(2) applies the nonbanking restrictions of Section 4(c)(8) whenever a bank holding company "engage[s] in any activities" not otherwise authorized by Section 4(a)(2). That extremely broad statutory language reaches every conceivable holding company act, including directing and profiting from a subsidiary bank's insurance activities. That conclusion is confirmed by Section 4(c)(8), which (i) sets forth the prohibition on insurance activities, (ii) is incorporated by reference into Section 4(a)(2), and (iii) as the lower court recognized, uses terms, here the words "company" and "affiliate," that include both banks and nonbanks.[8]

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[8] The court found the statutory language to be unclear largely because it accepted the Board's argument that petitioners' reading of the statutory language would override section 4(c)(14), which authorizes a bank holding company to own an export company. 12 U.S.C. § 1843(c)(14). These petitioners had explained, however, that the export provision falls within the express language of an exception to section 4(a)(2) that permits bank holding companies

Second, only the petitioners' interpretation comports with the acknowledged purpose of Section 4: "'to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity.'" App. A at 10a (quoting *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980)). That was obvious to the lower court, which described the Board's approach as "perplexing," noted the "apparent awkwardness and perhaps illogic," of the Board's view, and expressed "wonder" at the effect of the Board's interpretation. App. A at 15a. By contrast, the petitioners' "position has the virtue of consistency in reading the Act to preclude nonbank activities throughout a bank holding company's system." *Id.*

The lower court ultimately concluded, however, that Congress may have "adjusted the competing positions of strong forces with a compromise of imperfect symmetry." *Id.* That justification for the Board order, however, bases deference on mere speculation; neither the Court nor the Board relied upon any "competing position" that may have forced a legislative "compromise." The lower court's reliance on this Court's analysis in *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 374 (1986), *see* App. A at 15a, was thus inapposite.[9]

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to manage and control all subsidiaries "authorized under this Act." 12 U.S.C. § 1843(a)(2)(A). That which is authorized by section 4(c)(14) is, therefore, permissible under Section 4(a)(2). The insurance activities at issue here are not only not authorized, they are forbidden by the Act.

[9] In the *Dimension Financial* case, this Court reversed a Board interpretation that violated the plain language of the Act, even though it arguably furthered a legislative purpose. Unlike that case, here the petitioners do not invoke the "'plain purpose' of legislation at the expense of the terms of the statute itself." 474 U.S. at 374. Rather, the Board's interpretation conflicts with both the plain language and the express legislative purpose.

Third, the competing Board view cannot be squared with any statutory language or congressional intent. The Board does not contend that all state-chartered banks or all entities regulated by state banking authorities lie beyond its jurisdiction. To the contrary, the Board acknowledged that the nonbanking limitations apply if (i) a state-chartered bank is itself a parent bank holding company, (ii) a state-chartered bank is being used to "evade" the purposes of the Act, *see Citicorp (South Dakota)*, 71 Fed. Res. Bull. 789 (1985), or (iii) the nonbanking activities are being conducted in a nonbanking subsidiary of a state-chartered subsidiary bank. There is no evidence, and the Board supplied none, to support the view that Congress wished the insurance prohibition of Section 4(c)(8) to apply to entities subject to state banking regulation only some of the time. That the nonbanking limitations of the BHCA overlap—in at least these three, Board-acknowledged circumstances—with state banking regulation further demonstrates that exclusive state control of state-regulated entities was not a purpose of the Act. To take but one example, the Board supplied no indicia of statutory intent to support the view that Congress intended the insurance prohibition to apply only when the Board concluded that a state-chartered bank was being used to "evade" the BHCA and not when, as in this case, insurance activities are moved into a state-chartered bank expressly to avoid application of the Act.

The failure of the Board to advance a consistent view of the statutory structure as a whole weighs heavily against adoption of its analysis. *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 858 n.25 (1975). Thus, as former Board Governor Rice concluded, "the terms, structure, legislative history and purpose of the Act make clear that a bank holding company may not avoid the nonbanking restrictions of the Act by conducting these activities through a subsidiary bank". *Citicorp (South*

Dakota), 71 Fed. Res. Bull. 789, 792 (1985) (Rice, concurring).[10]

CONCLUSION

For the reasons stated herein, the petitioners respectfully request that the petition for a writ of certiorari be granted.

Respectfully submitted,

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April 18, 1990

[10] The court below derived some comfort from this Court's decision in *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981), which states, in part, that the "authority of . . . state member banks to furnish investment advisory services does not derive from the Board's regulation," but rather, that its scope "is to be determined by a particular bank's primary supervisory agency." App. A at 18a. The lower court failed to recognize, however, that the quoted footnote goes on to uphold the "imposition of restrictions on banks [that] prevented bank holding companies and their nonbanking subsidiaries from evading the restrictions by allowing the subsidiary banks to perform the restricted activities." *Id.*; *see* n.4 *supra*. That sort of evasion is exactly what is at issue here.

APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 1243—August Term 1988

Argued: June 1, 1989 Decided: November 29, 1989

Docket No. 89-4030

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., NEW YORK STATE ASSOC. OF LIFE UNDERWRITERS, AND PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,
Petitioners,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent,

MERCHANTS NATIONAL CORPORATION, THE NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, THE NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, AND THE NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS,
Intervenors.

Before:

KAUFMAN, NEWMAN, and MINER,
Circuit Judges.

Petition for review of an order of the Federal Reserve Board permitting two bank subsidiaries of a bank holding company to sell insurance.

Petition denied.

JONATHAN B. SALLET, Wash., D.C. (Jay L. Alexander, Lisa D. Burget, Miller, Cassidy, Larroca & Lewin, Wash., D.C., on the brief), *for petitioners and insurance-agent intervenors.*

DOUGLAS B. JORDAN, Senior Atty., Board of Governors of Fed. Reserve System, Wash., D.C. (John R. Bolton, Asst. Atty. Gen., U.S. Dept. of Justice; J. Virgil Mattingly, Gen. Counsel, Richard M. Ashton, Assoc. Gen. Counsel, Board of Governors of Fed. Reserve System, Wash., D.C., on the brief), *for respondent.*

JAMES A. MCDERMOTT, Indianapolis, Ind. (Stanley C. Fickle, Barnes & Thornburg, Indianapolis, Ind., on the brief), *for intervenor Merchants National Corp.*

(Paul B. Galvani, Martin E. Lybecker, William L. Patton, Alan G. Priest, Mark P. Szpak, Ropes & Gray, Wash., D.C.; Laurene K. Janik, Natl. Ass'n of Realtors, Chicago, Ill., *submitted a brief for amici curiae Insurance Company Associations and National Association of Realtors.*)

(Robert M. Kurucza, Robert G. Ballen, Steven S. Rosenthal, Debra L. Lagapa, Leslie J. Cloutier, Morrison & Foerster, Wash., D.C., *submitted a brief for amicus curiae California Bankers Clearing House Association.*)

(Ernest Gellhorn, Robert C. Jones, Jones, Day, Reavis & Pogue, Wash., D.C., *submitted a brief for amici curiae Conference of State Bank Supervisors, Independent Bankers Ass'n of America, and National Council of Savings Institutions.*)

(John J. Gill, Michael F. Crotty, American Bankers Ass'n, Wash., D.C.; James T. McIntyre, Jr., Randi S.

Field, McNair Law Firm, Wash., D.C.; Richard Whiting, Ass'n of Bank Holding Companies, Wash., D.C.; Charles L. Marinaccio, Kelley, Drye & Warren, Wash., D.C., *submitted a brief for amici curiae American Bankers Association, Association of Bank Holding Companies, Insurance/Financial Affiliates of America, and Association of Reserve City Bankers.*)

(Linley E. Pearson, Atty. Gen., Samuel L. Bolinger, Deputy Atty. Gen., Indianapolis, Ind., *submitted a brief for amicus curiae Indiana Department of Financial Institutions.*)

JON O. NEWMAN, *Circuit Judge*:

The extent to which banks should be permitted to engage in nonbanking activities is a major controversy in this country, attracting the increasing attention of Congress, administrative agencies, and courts. This petition for review of an order of the Board of Governors of the Federal Reserve System ("the Board" or "the Fed") brings before us one facet of that controversy. The issue is whether the Fed was entitled to conclude that section 4 of the Bank Holding Company Act of 1956 ("the Act" or "BHCA") does not restrict bank subsidiaries of a bank holding company from selling insurance. The issue arises on a petition filed by the Independent Insurance Agents of American ("IIAA") challenging the Board's March 3, 1989, order, which permitted two Indiana state banks acquired by the Merchants National Corporation, a bank holding company, to resume specified insurance activities permitted under Indiana law. *Merchants National Corp.*, 75 Fed. Res. Bull. 388 (1989) ("*Merchants II*"). The Board's order rested upon a determination that the nonbanking prohibitions of section 4 of the Act, as amended, 12 U.S.C. § 1843 (1988), do not apply to the activities of the bank subsidiaries of a bank holding company. Concluding that this construction of section 4 is within the

range of reasonable interpretation that the pertinent administrative agency is entitled to make, we deny the petition for review and leave this long-simmering controversy for such further consideration as Congress cares to give it.

Background

Litigation history. This matter is before this Court for the second time. On the prior occasion, we granted IIAA's petition for review after concluding, contrary to the Board's prior decision in this matter, *Merchants National Corp.*, 73 Fed. Res. Bull. 876 (1987) (*"Merchants I"*), that the Board's authority to permit insurance activities by the bank subsidiaries of Merchants National was temporarily precluded by the moratorium provisions of the Competitive Equality Banking Act of 1987 ("CEBA"), Pub. L. No. 100-86, 101 Stat. 552 (1987), *reprinted in* 12 U.S.C. § 1841 note (1988). *See Independent Insurance Agents of America, Inc. v. Board of Governors*, 838 F.2d 627, 633-34 (2d Cir. 1988). The moratorium, which was effective from March 6, 1987, to March 1, 1988, prohibited the Fed from issuing any order "that would have the effect of increasing the insurance powers" of a bank holding company or its banking or nonbanking subsidiaries. CEBA § 201(b)(3).

In anticipation of the expiration of the moratorium, Merchants National renewed its request that the Board authorize its Indiana banking subsidiaries to engage in insurance activities. After providing notice of this request, 52 Fed. Reg. 8966 (1987), and assessing the comments that were received, the Board issued the order that is the subject of the pending petition for review. This Court granted a stay of the order pending oral argument and continued the stay pending decision.

The statutory framework. Before introducing the facts, it will be helpful to outline briefly the pertinent statutory provisions of the Bank Holding Company Act.

The principal regulatory powers of the Fed concerning bank holding companies are set forth in sections 3 and 4 of the Act. 12 U.S.C. §§ 1842, 1843. Section 3 requires Board approval of the acquisition of ownership or control of any bank by a bank holding company, with narrow exceptions not here relevant. Section 3 sets forth factors governing acquisition approval, focusing on the competitive effect of the proposed acquisition, the financial and managerial resources of both the holding company and the acquired bank, and the convenience and needs of the community served. 12 U.S.C. § 1842(c).

Section 4 of the Act, the focal point of the Board's order in this case, contains two sets of prohibitions. First, it specifies, in what might be called the "ownership clause," that a bank holding company may not "retain direct or indirect ownership or control of any voting shares of any company which is not a bank or bank holding company." 12 U.S.C. § 1843(a)(2). Second, it provides, in what might be called the "activities clause," that a bank holding company may not "engage in any activities other than (A) those of banking or of managing or controlling banks . . . and (B) those permitted under [section 4(c)(8) of the Act] . . . ." *Id.* Section 4(c)(8) sets forth the so-called "closely related to banking" exception to the nonbanking provision. *Id.* § 1843(c)(8). In relevant part, section 4(c)(8) states that the section 4(a) nonbanking prohibitions shall not bar ownership by a bank holding company of:

> shares of any company the activities of which the Board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto, but for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to provide insurance as a principal, agent or broker . . . .

Id.

Facts. A number of states, including Indiana,[1] historically have authorized state-chartered banks to provide insurance services to their customers. On July 1, 1986, Merchants National Corporation, a bank holding company within the meaning of the BHCA, 12 U.S.C. § 1841(a), sought permission from the Fed to acquire the stock of two banks chartered under the laws of the State of Indiana, the Anderson Banking Company ("Anderson Bank") and the Mid State Bank of Hendricks County ("Mid State Bank"). Both of these state banks had engaged in general insurance activities prior to the date of Merchants National's applications, Anderson Bank directly since its incorporation in 1916, and Mid State Bank since its purchase of an insurance agency in 1985. Merchants National subsequently made a commitment that Mid State Bank would transfer to itself all insurance activities from its insurance agency subsidiary and thereafter conduct all such activities directly in the bank.

The initial Merchants National applications were protested by various insurance industry trade groups, including the IIAA, on the ground that the provisions of section 4 of the Act apply to the insurance activities of state banks owned by bank holding companies and therefore that the acquisitions of Anderson Bank and Mid State Bank could not be approved without termination of their insurance activities to the extent required under section 4. In response to the protests, Merchants National committed that it would cause the banks to divest their insurance agency activities within two years unless, within that time, it received Board approval for the banks to retain their insurance activities. Merchants National agreed that, prior to such approval, the banks would limit their insurance activities to the renewal of

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[1] Ind. Code § 28-1-11-2 provides: "Any bank or trust company shall have power . . . to solicit and write insurance as agent or broker for any insurance company authorized to do business in this state, other than a life insurance company."

existing policies. In light of these commitments, the Board approved the applications on October 29, 1986. 72 Fed. Res. Bull. 838 (1986).

On February 5, 1987, Merchants National filed an application seeking Board approval for Anderson Bank and Mid State Bank to resume the insurance activities that had just been suspended pursuant to the acquisition commitments. Merchants National sought permission on two alternative grounds. First, it contended that Anderson Bank and Mid State Bank were exempt from the insurance provisions of section 4 of the Act pursuant to the "grandfather" provision of section 4(c)(8)(D), as amended, 12 U.S.C. § 1843(c)(8)(D), under which a bank holding company or any of its subsidiaries is permitted to engage in insurance agency activity in which the holding company or the subsidiary was engaged on May 1, 1982, subject to certain geographical and functional limitations. Second, Merchants National sought more broadly a determination that the nonbanking prohibitions of section 4 of the Act do not apply to activities conducted directly by banking subsidiaries of a bank holding company. In *Merchants I*, the Board rejected the first contention but agreed with the second one. After the prior appeal to this Court and the expiration of the moratorium, the Board issued the decision challenged on this petition for review. *Merchants II*.

The Board's Decision

The core of the Board's decision in *Merchants II* was its conclusion, previously expressed in *Merchants I*, that the provisions of section 4 limiting the nonbanking activities of bank holding companies do not apply to bank subsidiaries of a bank holding company. Consistent with this view, the Board also ruled, as it had in *Merchants I*, that section 4's prohibition upon a bank holding company's acquisition of a nonbanking entity (unless that entity engages only in activities "closely related to bank-

ing") does not apply to a holding company's acquisition of a bank. The Board recognized an exception to this latter conclusion in those instances, illustrated by the *Citicorp (South Dakota)* case, 71 Fed. Res. Bull. 789 (1985), where the Board finds an evasion arising from a holding company's acquisition of an entity that purports to be a "bank" but engages in insignificant banking activities, indicating that the acquisition is "primarily, if not solely" for the purpose of enabling the holding company to engage in the target's nonbanking activities.[2] *Merchants II*, Fed. Res. slip op. at 8 n.11.

The Board grounded its conclusions on several considerations. First, the Board pointed out that the limitations of section 4(a)(2) apply in express terms to "bank holding companies," not to "banks." *Id.* at 11. Second, the Board relied on what it considered a structural argument: the "ownership clause" of section 4 restricts the entities that a bank holding company may acquire or retain, and the "activities clause" restricts the activities that the bank holding company itself may engage in. In the Board's view, if the restriction on activities applied to the activities of subsidiaries of a bank holding company, the restriction on acquisition or retention of nonbank entities would be superfluous. *Id.* at 11-13. Third, the Board emphasized that the restriction on acquisition or retention was broadly phrased to prohibit "direct or indirect" ownership, whereas the restriction on engaging in activities omitted the comparable adverbs "directly or indirectly," words the Board appears to acknowledge would have made the restrictions of section 4 applicable

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[2] The Board decided *Citicorp* in the exercise of its authority under section 5 of the Act, 12 U.S.C. § 1844. The Supreme Court subsequently ruled that section 5 "only permits the Board to police within the boundaries of the Act." *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 373 n.6 (1986). We do not decide whether, in light of *Dimension Financial*, *Citicorp* was a proper exercise of the Commission's authority under section 5 or any other provision of the Act.

to activities of a bank holding company's subsidiaries. *Id.* at 12-13. Fourth, the Board asserted that since the enactment of the Bank Holding Company Act, it has consistently declined to read the activities restriction of section 4 as applicable to bank subsidiaries of a bank holding company. *Id.* at 15-16. Fifth, the Board found in the legislative history of the Bank Holding Company Act and its subsequent amendments a congressional purpose to leave the scope of permissible activities of bank subsidiaries of a bank holding company subject only to the authority that issued the banks' charter, without any further restriction for the Act itself.[3] *Id.* at 17-20.

The Board also reckoned with and rejected an argument based on section 101(d) of CEBA, which amends section 3 of BHCA to permit qualified state-chartered savings banks to engage in any activity permitted by state law, but prohibits such banks from violating the insurance restrictions of section 4(c)(8). 12 U.S.C.

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[3] Though concluding that the provisions of section 4 do not apply to bank subsidiaries of a holding company, the Board somewhat inconsistently also concluded, as it had in *Merchants I*, that neither Anderson Bank nor Mid State Bank qualifies under the grandfather provision of the Garn-St. Germain Act, which is section 4(c)(8)(D) of the Bank Holding Company Act. The Board pointed out that Anderson Bank did not become a subsidiary of a bank holding company and Mid State Bank did not start selling insurance until after the May 1, 1982, grandfather date. If, as the Board concluded, section 4 is inapplicable to bank subsidiaries of a bank holding company, it is not readily apparent why the grandfather clause of section 4(c)(8) was inapplicable on the narrow ground that its precise terms were not met, rather than the broader ground that section 4, to which the clause is an exception, has no application to banking subsidiaries. Indeed, it is the Board's position that "the Garn-St. Germain Act has no applicability to situations . . . where the nonbanking provisions of section 4 of the [Bank Holding Company] Act do not apply." *Merchants II*, Fed. Res. slip op. at 8 n.10. Perhaps the Board simply felt it prudent to reckon with the first of Merchant National's alternative arguments and reject it on a narrow ground before proceeding to the second argument, which presented the broader ground.

§ 1842(f). It was contended that if section 4 did not restrict the nonbanking activities of bank subsidiaries of a bank holding company, an exemption for savings banks would not have been necessary. The Board responded that this amendment may have been adopted to confirm the Board's view in the face of arguments advanced by insurance trade associations and to provide special limitations applicable only to savings bank subsidiaries of a bank holding company. In this connection, the Board emphasized that Congress had considered and declined to enact legislation to extend the restrictions on savings bank subsidiaries to all bank subsidiaries of a bank holding company. *Merchants II*, Fed. Res. slip op. at 23-24; *see* H.R. Conf. Rep. No. 261, 100th Cong., 1st Sess. 130 (1987); S. Rep. No. 19, 100th Cong., 1st Sess. 33 (1987).

Finally, the Board noted that its decision leaving the activities of bank subsidiaries to regulation by the chartering authority applied only to activities carried on directly by those banks and did not insulate from section 4 the activities of subsidiaries of the bank subsidiaries. This application of section 4 to third generation entities, those owned by the subsidiaries of a bank holding company, was based on section 2(g)(1) of the Act, 12 U.S.C. § 1841(g)(1), which provides that shares of such third generation entities are deemed to be held indirectly by the bank holding company; as a result, whether such entities may be owned by a subsidiary of a bank holding company is governed, in the Board's view, by section 4's limitation on entities that may be owned by a bank holding company. *Merchants II*, Fed. Res. slip op. at 25.

Discussion

There can be no doubt that the Bank Holding Company Act is "intended to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity." *See Lewis v. BT Invest-*

ment Managers, Inc., 447 U.S. 27, 46 (1980). What is less clear is the extent to which Congress has decided to implement that policy. IIAA contends that Congress has required a nearly complete separation of banking and nonbanking activities, precluding bank holding companies and all entities within their systems from engaging in nonbanking activities other than the "closely related to banking" activities specifically identified in section 4(c)(8) of the Act. The Board believes that Congress has not gone so far. In its view, Congress required a significant degree of separation with respect to bank holding companies themselves, but did not wish to displace the traditional authority of state and national bank chartering authorities to determine what nonbanking activities could appropriately be engaged in by banks that are subject to their jurisdiction, even though such banks were owned by a bank holding company under the jurisdiction of the Fed.

In resolving this dispute, we must keep in mind that we are not making an initial construction of a statute, but rather reviewing a construction made by an expert regulatory agency. In that context, our task is to determine whether Congress has "directly spoken to the precise question at issue," and, if so, to give effect to any "unambiguously expressed intent of Congress," or, if not, to determine "whether the agency's answer is based on a permissible construction of the statute." *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984). Though both sides support their views of the statute by relying on some of the statutory language, we cannot say that the provisions of the Act reveal an unambiguous congressional intent concerning the precise question at issue. We find no provision that says, in substance, "The Board may not regulate the activities of bank subsidiaries of bank holding companies," or "Bank subsidiaries of bank holding companies may engage in nonbank activities to the extent permitted

by their chartering authorities." The Board reads the Act as if it contained such language. On the other hand, we find no provision that says, in substance, "Bank subsidiaries of bank holding companies may not engage in nonbank activities." The IIAA reads the Act as if it contained this wording. The question for us is whether the Board's interpretation of the language that does appear in the Act is reasonable, an inquiry we undertake by examining all relevant sources, including such clues as the statutory language may provide.

Both sides claim that the text of the Act supports their interpretations, and each can find some, but not overwhelming, support in various words and phrases. As the Board noted in its decision, the limitations of section 4(a)(2) apply in terms to "bank holding companies," not to "banks." However, that observation somewhat begs the question, which is whether the limitations upon bank holding companies should be interpreted to restrict the activities those entities may engage in *indirectly* through their banking subsidiaries. Of similarly little, if any weight, is the argument that because the "ownership clause" of section 4(a)(2) does not bar a bank holding company from owning subsidiary banks, the "activities clause" should be interpreted not to apply to activities of subsidiary banks. The argument is a *non sequitur*. It would be entirely sensible for Congress, if it wished, to bar a bank holding company from owning nonbanks and also prohibit a bank holding company from engaging indirectly in nonbank activities conducted by its bank subsidiaries. For its part, the IIAA points to the language prohibiting bank holding companies from engaging in nonbank activities and assumes that this language means "engage in directly or through subsidiaries."

Somewhat more supportive of the Board's position are textual arguments arising from comparisons of the "activities clause" with other language in section 4(a)(2). First, the grandfather proviso of section 4(a)(2)

permits a bank holding company to engage in those activities "in which directly or through a subsidiary" it was engaged in at designated times and under designated circumstances. The Board points out that no similar phrase modifies the "activities clause." Second, the "ownership clause" prohibits the retention of "direct or indirect" ownership of nonbanks, and no similar phrase modifies the prohibition on engaging in nonbank activities. The use of these phrases in section 4(a)(2) and their absence from the "activities clause" might imply a deliberate congressional choice not to restrict the activities of bank subsidiaries, *cf. Russello v. United States*, 464 U.S. 16, 23 (1983) (significance of different wording in statute), but might also result from drafting different clauses at different times and assembling them without intending differences in phrasing to have significance.

The Board derives a somewhat stronger argument for its interpretation from the structure of the Act. It points out that if the "activities clause" applied to subsidiaries of a bank holding company, the "ownership clause" would be virtually superfluous, since, under that reading, the "activities clause" alone would preclude a bank holding company from owning a nonbank. Moreover, as the Board further points out, such a reading would appear to create some internal inconsistencies. For example, section 4(c)(14) permits a bank holding company, under specified circumstances, to own an export trading company; however, this would be prohibited if the "activities clause" applied to subsidiaries of a bank holding company since that clause exempts only the "closely related to banking" activities set forth in section 4(c)(8), which do not include export trading. IIAA's only response is that the (c)(14) exemption would control over the (a)(2) "activities clause" since it comes later in the statute. *See Lodge 1858 v. Webb*, 580 F.2d 496, 510 (D.C. Cir.), *cert. denied*, 439 U.S. 927 (1978). That canon of construction may sometimes be helpful in resolving irrecon-

cilable inconsistencies, but it need not be invoked where the statute may be interpreted to avoid the inconsistency in the first place.

However, IIAA also finds support for its interpretation in the structure of section 4. As IIAA points out, section 4(c)(8), establishing the circumstances for exempting various entities from the restrictions of section 4, including the "activities clause" of section 4(a)(2), uses the term "company" to describe those entities, and "company" is defined by section 2(b) broadly enough to include a bank. *See* 12 U.S.C. § 1841(b). Moreover, section 4(c)(8) instructs the Board, in deciding whether a particular activity is "a proper incident to banking," to assess whether the performance of that activity "by an affiliate of a holding company" will produce public benefits, and "affiliate" is defined by section 2(k) to include a "company" and, hence, a bank. *See* 12 U.S.C. § 1841(k). The available inference is that subsidiary banks are subject to the "activities clause" because they are within the category of entities exempted from that clause by section 4(c)(8).

Perhaps the most perplexing aspect of the structural arguments concerns the Board's contention that though it has no authority to preclude bank subsidiaries of a bank holding company from engaging in nonbank activities, it does have authority to preclude the subsidiaries of a bank subsidiary from engaging in nonbank activities. Thus, the Board adopts a generation-skipping approach: It may prohibit nonbank activities by bank holding companies and by their "grandchildren," *i.e.*, the subsidiaries of their bank subsidiaries, but not by their bank "children," *i.e.*, the holding companies' immediate bank subsidiaries. The Board's rationale is that the prohibition in the "ownership clause" on "direct or indirect" ownership of nonbank entities precludes a bank holding company from indirectly owning the nonbank subsidiary of its own bank subsidiary.

This contention elicits conflicting responses from IIAA and Merchants National. IIAA contends that the Fed can prohibit nonbanking activities at all three levels and cites the apparent awkwardness and perhaps illogic of the Board's generation-skipping approach as evidence that the Board's interpretation of the "activities clause" is incorrect. As IIAA points out, under the Board's reading of section 4(a)(2), a holding company's bank subsidiary that owns a nonbank subsidiary can escape the prohibition of the "ownership clause" by merging the "grandchild" into the bank subsidiary and operating the nonbank activities itself. That is precisely what Mid-State Bank did in this proceeding. For its part, Merchants National argues that the Fed may bar nonbanking activities only of a holding company itself and may not preclude those of either second generation bank subsidiaries or their third generation subsidiaries.

IIAA's position has the virtue of consistency in reading the Act to preclude nonbank activities throughout a bank holding company's system. Moreover, if the Board is correct that Congress wished to leave the activities of bank subsidiaries subject to the regulation of only their chartering authorities, one is left to wonder why those authorities were not relied on to control all of a bank subsidiary's activities, whether conducted directly by the bank subsidiary itself or indirectly through its own subsidiary. On the other hand, if the Board is right that the Act leaves the nonbank activities of bank subsidiaries within the control of bank chartering authorities but precludes nonbank activities by holding companies and by the subsidiaries of their bank subsidiaries, this would not be the first time that Congress has adjusted the competing positions of strong forces with a compromise of imperfect symmetry. *See Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 374 (1986). We think it prudent not to resolve the issue of the Board's authority over the nonbank activities of subsidiaries of bank subsidiaries until that issue is squarely presented.

IIAA endeavors to support its interpretation of the "activities clause" with isolated quotations from the legislative history of the Act. Some members of Congress expressed the view that the Act was intended to keep "banks" out of nonbank activities. As Congressman O'Hara put it, "I do not think, however, that any of my colleagues will question the soundness of the rule that banks should stick exclusively to banking and should be as free of nonbanking interests as C[æ]sar's wife from suspicion." 101 Cong. Rec. 8033 (1955). *See also* 102 Cong. Rec. 6853 (1956) (statement of Sen. Barkley); 101 Cong. Rec. 8030 (1955) (statement of Rep. Rains); *id.* at 8035 (statement of Rep. Multer); *id.* at 8184 (statement of Rep. Smith).

These remarks do not provide unambiguous support for IIAA's interpretation for several reasons. First, in some instances, it is not clear if the legislator is referring to bank subsidiaries of bank holding companies or to the holding companies themselves. Second, many expressions condemning nonbank activities, including one that explicitly mentions banks and bank holding companies, *see* 102 Cong. Rec. 6853 (1956) (statement of Sen. Barkley), focus on ownership interests, rather than the business activities that a bank subsidiary may conduct. Plainly, as the "ownership clause' commands, Congress did not want bank holding companies to own nonbanks. The legislative history, however, is remarkably free of clear statements indicating disapproval of nonbanking activities engaged in directly by bank subsidiaries. If such were the intent of Congress, one would expect to find a clear statement of such purpose in the key House and Senate reports. Finally, during the hearings the attention of Congress was specifically called to the range of activities that state chartering authorities were permitting for bank subsidiaries of bank holding companies, *see Control and Regulation of Bank Holding Companies: Hearings on H.R. 2674 Before the House Comm. on Banking and Currency*, 84th Cong., 1st Sess. 536, 553 (1955) (testi-

mony of Ellery C. Huntington), and some Congressmen expressed the view that the holding company bill would not modify such state regulatory authority, *id.* at 553 (statements of Rep. Spence and Rep. Brown).

Subsequent legislative forays into the field, though an uncertain source of prior congressional intent at best, *see Russello v. United States*, 464 U.S. at 26, reveal primarily that Congress finds this a difficult area in which to provide clear answers. In connection with the 1970 amendments to the Act, the House Committee on Banking and Currency reported a bill that, among other things, explicitly excluded insurance activities from the "closely related to banking" activities permitted under section 4(c)(8). H.R. Rep. No. 387, 91st Cong., 1st Sess. 9 (1969). Referring to the effect of this and another prohibition concerning sale of mutual funds, the Committee stated:

> It should be emphasized that these two prohibitions apply only to the bank holding company and its nonbanking subsidiaries and not to the bank subsidiaries of bank holding companies whose insurance agency and mutual fund operations are governed by other Federal and State laws. This is in keeping with the original concept of the 1956 act, which was to regulate bank holding companies and not subsidiary banks.

Id. at 15. The House then went further and amended the bill to identify a list of activities explicitly prohibited both to bank holding companies and all of their subsidiaries, including banks. 115 Cong. Rec. 33133-35. The Senate disagreed with this approach, *see* S. Rep. No. 1084, 91st Cong., 2d Sess. 12-16 (1970), and it was rejected in conference. H.R. Conf. Rep. No. 1447, 91st Cong., 2d Sess. 13-16 (1970).

Finally with respect to subsequent legislative attention, some significance must be attached to the fact that Con-

gress specifically called to its own attention the correctness of the Board's interpretation of the "activities clause" in *Merchants I* by enacting the moratorium provisions of CEBA and providing itself with a one-year opportunity to determine whether to legislate contrary to the Board's view. The moratorium expired without the passage of new legislation on this subject.

Case law has not directly focused on the issue now before us, but two decisions provide the Board with some comfort. When investment companies challenged the Board's determination that the services of an investment adviser to a closed-end investment company were "closely related to banking" under section 4(c)(8), they argued that the Board was allowing subsidiary banks to render such services. *See Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981). The Supreme Court disagreed and noted with apparent approval the Board's view that whether such services could be rendered by subsidiary banks depended solely on the decisions of their chartering authorities:

> The simple answer to this argument is that not only does the interpretive ruling confer no authorization to undertake any activities, but also the Board does not have the power to confer such authorization on banks. As the Board's opinion in this case stated:
>
> "[T]he Board's regulation . . . authorizes investment advisory activity to be conducted by a nonbanking subsidiary of the holding company. The authority of national banks or state member banks to furnish investment advisory services does not derive from the Board's regulation; such authority would exist independently of the Board's regulation and its scope is to be determined by a particular bank's primary supervisory agency."

Id. Tilting in the same direction is *Cameron Financial Corp. v. Board of Governors*, 497 F.2d 841, 848 (4th Cir.

1974), which ruled that a bank subsidiary is not included within the term "subsidiary" for purposes of the grandfather provisions of section 4(a).

After assessing all of the relevant considerations, we are satisfied that the Board, acting within its sphere of competence, has made a reasonable interpretation of section 4(a)(2), one that confides decisions concerning the scope of insurance and other nonbank activities of bank subsidiaries to their national and state chartering authorities. If that interpretation is to be altered, Congress will have to enact suitable legislation.

The petition for review is denied.

APPENDIX B

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 1st day of June one thousand nine hundred and eighty-nine.

Present: HON. IRVING R. KAUFMAN,

HON. JON O. NEWMAN,

HON. ROGER J. MINER, *Circuit Judges.*

Docket No. 89-4030

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., *et al.*,
Petitioners,

-v-

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent.

[Filed June 1, 1989]

It is hereby ordered that the stay previously granted by this court shall continue pending disposition of the appeal.

ELAINE B. GOLDSMITH
Clerk

By: /s/ Arthur Heller
ARTHUR HELLER
Deputy Clerk

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty eighth day of March one thousand nine hundred and eighty-nine.

Present: HON. WILFRED FEINBERG

HON. LAWRENCE W. PIERCE, Circuit Judges

HON. CONSTANCE BAKER MOTLEY, District Judge

Docket No. 89-4030

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., *et al.*,
Petitioners,

-v-

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent.

[Filed Mar. 28, 1989]

It is hereby ordered that the motion for a stay be and it hereby is GRANTED only until argument of the appeal.

The present scheduling order shall remain in effect.

ELAINE B. GOLDSMITH
Clerk

By: /s/ Edward J. Guardaro
EDWARD J. GUARDARO
Deputy Clerk

APPENDIX C

75 Fed. Res. Bull. 388 (1989)

FEDERAL RESERVE SYSTEM

Merchants National Corporation
Indianapolis, Indiana

Order Granting Relief From Commitments Regarding Insurance Agency Activities of Subsidiary Banks

Merchants National Corporation, Indianapolis, Indiana ("Merchants"), a bank holding company within the meaning of the Bank Holding Company Act ("BHC Act" or "Act"), has applied under section 4(c)(8)(D) of the BHC Act (12 U.S.C. § 1843(c)(8)(D)) and section 225.25(b)(8)(iv) of the Board's Regulation Y (12 C.F.R. § 225.25(b)(8)(iv)) for approval for its wholly owned subsidiary, Anderson Banking Company, Anderson, Indiana ("Anderson Bank"), to resume the conduct of certain insurance agency activities authorized for state banks under Indiana law. Alternatively, Merchants seeks a Board determination that the nonbanking prohibitions of section 4 of the BHC Act do not apply to activities conducted directly by subsidiary banks of a bank holding company, thereby permitting Anderson Bank and another of Merchant's state bank subsidiaries, Mid State Bank of Hendricks County, Danville, Indiana ("Mid State Bank"), to resume insurance agency activities. In both cases the insurance agency activities would be conducted directly by the banks and not through subsidiaries of the banks.

I. *Background*

The record shows that Anderson Bank, prior to its acquisition by Merchants, engaged directly in insurance agency activities since the bank's incorporation in 1916

and that Mid State Bank acquired an insurance agency in 1985.[1] The banks are authorized to sell insurance directly pursuant to state law.[2]

On October 29, 1986, the Board approved applications by Merchants under section 3 of the BHC Act to acquire Anderson Bank and Mid State Bank. 72 Federal Reserve Bulletin 838 (1986). The applications had been protested by various insurance industry trade groups on the ground that, as subsidiaries of a bank holding company, the insurance agency activities then being conducted by the banks pursuant to Indiana law would be prohibited by section 4 of the BHC Act, as amended by Title VI of the Garn-St Germain Depository Institutions Act of 1982.[3] As discussed below, the Garn-St Germain Act amended section 4(c)(8) of the BHC Act to provide that, with seven specific exceptions, insurance activities are not closely related to banking. This amendment removed the Board's discretion to authorize insurance activities as a permissible nonbanking activity for bank holding companies under the closely related to banking standard of section 4(c)(8) of the Act.

In response to the protests, Merchants committed that, unless it received Board approval in the meantime for the banks to retain their insurance activities, it would cause the banks to divest the insurance agency activities within two years and, in the interim, to refrain from the sale of insurance except for the renewal of existing poli-

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[1] Prior to consummation of this proposal, Mid State Bank will transfer the insurance activities of the subsidiary to the bank itself, which will thereafter conduct the activities directly. Anderson Bank and Mid State Bank would act as agent for a full line of property and casualty coverage, but would not sell life insurance.

[2] Ind. Code § 28-1-11-2 provides that "any bank or trust company shall have power . . . to solicit and write insurance as agent or broker for any insurance company authorized to do business in this state, other than a life insurance company."

[3] Pub. L. No. 97-320, codified at 12 U.S.C. § 1843(c)(8).

cies. Merchants subsequently sought relief from these commitments. On September 10, 1987, the Board granted the requested relief on the grounds that the insurance activities would be conducted directly by the banks and, thus, would not be prohibited by section 4 of the BHC Act or consequently the insurance provisions of the Garn-St Germain Act. 73 Federal Reserve Bulletin 876 (1987). The Board's Order noted that the relief did not violate the moratorium provisions of the Competitive Equality Banking Act of 1987 ("CEBA")[4] because Merchants had acquired the banks involved before the moratorium. The Board also noted that the grant of relief would not increase the banks' insurance powers since the banks already had the powers by virtue of state law and those powers were not and never had been limited by the BHC Act.

Protestants sought review of the Board's decision in the United States Court of Appeals for the Second Circuit, which, on January 25, 1988, vacated the Board's Order.[5] The court ruled that the Board's decision fell within the moratorium provisions of CEBA and, thus, that the Board should not have granted Merchants's request to conduct the insurance activities while the moratorium was effective. The court did not address the question of whether insurance activities conducted directly by the banks would be prohibited by the nonbanking provisions of section 4 of the BHC Act. The moratorium provisions have now expired, and Merchants has requested that the Board reissue the vacated Order.[6]

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[4] Pub. L. No. 100-86, 101 Stat. 552 (1987).

[5] *Independent Insurance Agents of America, Inc.* v. *Board of Governors*, 838 F.2d 627 (2nd Cir. 1988).

[6] By letter dated December 8, 1988, the Board granted a request by Merchants for an extension of time to divest the insurance agency activities of Anderson Bank and Mid State Bank until such time as the Board acts on the request of Merchants to reissue its earlier Order.

Notice of the application, affording interested persons an opportunity to submit comments on the proposal, was published (52 *Federal Register* 8966 (1987)). The time for filing comments has expired, and the Board has considered the application and all comments received, including those of various insurance trade associations ("protestants").[7]

Protestants contend that the banks do not qualify under any of the seven exemptions to the insurance provisions in the Garn-St Germain Act and that, therefore, they may not resume their insurance agency activities. With respect to Merchants's alternative argument, protestants contend that the terms and legislative history of the BHC Act and the Board's regulations indicate that the nonbanking and insurance provisions of section 4 of the BHC Act apply to all bank holding company activities, including activities conducted by a subsidiary bank of the holding company. In protestants' view, a bank holding company's activities, whether conducted directly by the holding company or by any of its subsidiaries, including subsidiary banks, are limited by the terms of section 4 of the Act to "banking" activities and activities permitted under the closely related to banking standard in section 4(c)(8) of the Act (or one of the other specific exemptions in the Act, none of which are relevant here). Protestants argue that because Anderson Bank's and Mid State Bank's insurance activities are not "banking" and do not qualify under any of the insurance ex-

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[7] The Board has received comments protesting the application and the request to reissue the earlier Order from the Independent Insurance Agents of America, Inc., Independent Insurance Agents of New York, Inc., National Association of Casualty and Surety Agents, National Association of Life Underwriters, National Association of Professional Insurance Agents, National Association of Surety Bond Producers, New York Association of Life Underwriters, and Professional Insurance Agents of New York, Inc.

emptions in section 4(c)(8), Merchants may not engage in the activities through the banks.[8]

After considering the comments of all interested parties and for the reasons set forth below, the Board has determined to grant Merchants's request for relief from its earlier commitments on the alternative grounds advanced by Merchants, thereby permitting Anderson Bank and Mid State Bank to resume the insurance agency activities they terminated when they were acquired by Merchants in 1986.

II. *Inapplicability of Exemption D of the Garn St-Germain Act*

Initially, the Board has determined that Anderson Bank and Mid State Bank do not qualify under section 4(c)(8)(D), the grandfather provision of the Garn-St Germain Act (hereinafter "exemption D"), to engage in insurance agency activities. Exemption D permits a bank holding company or any of its subsidiaries to engage in any insurance agency activity in which the bank holding company or subsidiary was engaged on May 1, 1982, sub-

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[8] Protestants also argue that Merchants should be bound by its earlier commitments to divest the banks' insurance activities because Merchants voluntarily offered the commitments with full knowledge of their limitations and that, in any event, the commitments preclude Merchants from arguing that the provisions of section 4 of the BHC Act do not apply to the direct activities of the banks.

In the Board's view, however, the commitments contemplated that Merchants could request Board relief from the commitments. While couched in terms of seeking Board approval on the Board's application Form Y-4, the commitments did not represent a concession by Merchants that section 4 applies to the direct activities of the banks. Rather, the commitments contemplated that the application would provide a forum for evaluating the issues and arguments raised by the proposal apart from Merchants' earlier application to acquire the banks. Accordingly, the Board does not consider that the commitments limit either the right of Merchants to request relief or the arguments Merchants may put forward in support of that relief.

ject to certain geographic and functional limitations. Exemption D, however, applies only to entities that were bank holding companies or subsidiaries of bank holding companies on May 1, 1982. The record shows that on May 1, 1982, Anderson Bank was not a subsidiary of a bank holding company and, therefore, does not qualify under Exemption D. Similarly, Mid State Bank does not qualify under Exemption D because it did not commence selling insurance until after the May 1, 1982, grandfather date.[9]

III. *Inapplicability of the Nonbanking Provisions of the BHC Act to the Direct Activities of Holding Company Banks*

Accordingly, the Board has considered Merchants's alternative ground for relief. On the basis of the record before it and the comments received, the Board has determined that the direct insurance activities of Anderson Bank and Mid State Bank are not limited by the nonbanking provisions of section 4 of the BHC Act or, consequently, the insurance provisions of the Garn-St Germain Act.[10] In the Board's view, the nonbanking pro-

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[9] Mid State Bank appears to qualify for the exemption provided in section 4(c)(8)(C) of the BHC Act for insurance agency activities conducted in a town of less than 5,000 inhabitants. In this application, Merchants initially had proposed that Mid State Bank conduct the insurance agency activities through a wholly owned subsidiary under exemption C. Merchants, however, subsequently withdrew that request and amended the proposal to conduct the insurance activities directly by Mid State Bank on the basis discussed below that the nonbanking provisions of the BHC Act do not apply to the direct activities of holding company banks.

[10] As noted, Title VI of the Garn-St Germain Act does not establish a prohibition on the conduct of insurance activities by bank holding companies separate from or in addition to the general nonbanking prohibitions of section 4 of the BHC Act. Rather, Title VI limits the Board's discretion to authorize bank holding companies to conduct these activities under the closely related to banking exception (in section 4(c)(8) of the Act) to the general nonbanking provisions of the Act (in section 4(a)). Thus, the provisions of the

visions of section 4 do not limit the *direct* activities of holding company banks, except where the record demonstrates the type of evasion described in the *Citicorp (South Dakota)* case,[11] a situation not present in the instant case.[12] The Board believes this view is consistent with the terms, purposes, and legislative history of the BHC Act and the Board's regulations, prior interpretations, and longstanding practice.

A. *Terms and Structure of the BHC Act*

Section 4 of the BHC Act contains two provisions that together limit the nonbanking activities and investments of bank holding companies. First, section 4 prohibits, with certain specific exceptions, a bank holding company from acquiring or retaining, directly or indirectly, voting shares of any company except a bank.[13] The princi-

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Garn-St Germain Act have no applicability to situations, such as this, where the nonbanking provisions of section 4 of the Act do not apply.

[11] 71 Federal Reserve Bulletin 789 (1985). In that case, the Board found, based on the structure of the South Dakota statute, the operating plans of Citicorp, and the fact that the bank would serve primarily as an insurance subsidiary of Citicorp and would conduct only insignificant banking activities, that the acquisition of the bank was primarily, if not solely, for the purpose of enabling Citicorp to engage through the bank in various insurance activities. The Board did not address the question raised in this case regarding whether the prohibitions of section 4 of the Act apply to the direct activities of holding company banks where no evidence of evasion is presented.

[12] In this case, the record does not show, nor is there any allegation, that the banks would be operated by Merchants predominantly as insurance agencies or that the acquisition of the banks is a device to enable the applicant to engage in insurance activities. Rather, the record shows that the insurance activities of the banks are incidental and small relative to their banking operations.

[13] Section 4(a) of the Act provides:

> Except as otherwise provided in this Act, no bank holding company shall

pal exception to this prohibition is for the shares of companies engaged in activities that the Board has determined are closely related to banking. By its terms, this restriction in section 4 does not apply to shares of a company that is itself a bank. Thus, a bank holding company that controls an institution that qualifies as a "bank" under the definition in the Act [14] is not required, in order to acquire or retain the shares of the institution, to limit the institution's activities to those permitted under the closely related to banking standard of section 4 (or one of the other limited exceptions in the Act), except where the record demonstrates an evasion of the Act, such as presented in the *Citicorp* (*South Dakota*) case. It is only companies that do not qualify as "banks" under the Act that must limit their nonbanking activities to those permitted under the closely related to banking standard in section 4(c)(8) of the Act (or qualify under some other exception in section 4) in order to be acquired or retained directly or indirectly by a bank holding company.

In addition to the above limitation, section 4 of the Act provides that a bank holding company may not "engage in any activities other than . . . those of banking or of managing or controlling banks and other subsidiaries authorized under the Act or of furnishing services to or performing services for its subsidiaries" and activities the

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(1) . . . acquire direct or indirect ownership or control of any voting shares of any company *which is not a bank*, or

(2) . . . retain direct or indirect ownership or control of any voting shares of any company *which is not a bank* or bank holding company or engage in any activities other than (A) those of banking or of managing or controlling banks and other subsidiaries authorized under this Act or of furnishing services to or performing services for its subsidiaries, and (B) those permitted under paragraph (8) of subsection (c) of this section [the closely related to banking exception] . . . (emphasis supplied) 12 U.S.C. § 1843(a).

[14] 12 U.S.C. § 1841(c).

Board has determined to be closely related to banking. 12 U.S.C. § 1843(a)(2). Protestants contend that this provision applies not only to activities conducted directly by a bank holding company, but also to activities conducted indirectly through any subsidiary of the bank holding company, including a subsidiary bank. This interpretation, however, cannot be squared with the words or structure of the statute.

The language of the activities limitation in section 4(a)(2) forbids "bank holding companies"—not "banks"—from engaging in activities other than those specified in that provision. The BHC Act defines "bank holding company" to mean any company that has control over any bank,[15] a definition that clearly refers only to the parent holding company itself, not to the system as a whole or to any "subsidiary," a term that is separately defined.[16]

The structure of the BHC Act indicates that this provision of section 4(a)(2) of the Act was intended to apply to the activities of bank holding companies themselves, many of which are operating companies engaged directly in nonbanking activities as well as in controlling banks and companies engaged in permissible nonbanking activities.[17] This reading harmonizes the provisions of section 4 of the Act, with one provision limiting the types of companies the shares of which a bank holding company may acquire and retain (banks and other companies authorized under the Act), and the second limiting in a similar manner the activities in which the bank holding

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[15] 12 U.S.C. § 1841(a)(1).

[16] 12 U.S.C. § 1841(d).

[17] The portion of section 4 that authorizes a bank holding company to engage in "banking" is intended to provide for those few situations that existed in 1956 in which the bank holding company was itself a bank. *See* Heller, *Federal Bank Holding Company Law*, § 4.02(1).

company itself may engage to (1) banking, (2) managing and controlling banks and authorized nonbank companies, and (3) activities closely related to banking.

Furthermore, section 4(a) of the Act distinguishes between a bank holding company's acquiring and retaining "direct or indirect" ownership or control of any company that is not a bank, on the one hand, and the holding company's engaging in activities itself, on the other. The use of the words "direct or indirect" in the investment limitation of the Act makes clear that neither a bank holding company nor any of its subsidiaries may own or control a nonbank company (unless exempted). In the activities limitation of section 4(a)(2), however, Congress did not use the words "directly or indirectly" to modify the word "engage". This demonstrates, in the Board's view, Congress' intent to apply the activities limitation in section 4(a)(2) to the holding company only and not to its subsidiaries.[18]

The reading suggested by protestants would make superfluous the provision in section 4(a)(2) restricting the types of companies that may be controlled by bank holding companies to banks and authorized nonbanks. If a bank holding company is deemed to be engaged in each activity in which a company it controls is engaged, as protestants suggest, the other provision of section 4 prohibiting a bank holding company from controlling nonbank companies unless engaged in permissible activities

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[18] Protestants look to 12 U.S.C. § 1850, which establishes a competitor's standing to challenge adverse Board action regarding applications by bank holding companies to engage directly or indirectly in nonbanking activities, to demonstrate that the term "engage" in the BHC Act necessarily applies to the activities of a bank holding company and all its subsidiaries. In that section, however, the word "engage" is modified by the words "directly or indirectly." The activities limitation in section 4(a)(2), however, is not modified by the words "directly or indirectly."

would be unnecessary.[19] Accordingly, the Board believes that the provision of section 4(a)(2) of the Act limiting the activities in which a bank holding company may "engage" applies only to the activities of the bank holding company itself, and that activities of subsidiaries of the bank holding company are regulated through provisions limiting the companies that a bank holding company may hold the shares of or control to banks and other companies engaged in activities permitted for bank holding companies under the Act.

Protestants point to the fact that a bank may be a "subsidiary" of a bank holding company under the Act's definition as evidence that the Act does not distinguish between banking and nonbanking subsidiaries.[20] That conclusion simply does not follow, however. The Act clearly distinguishes between banking and nonbanking subsidiaries in section 4(a) when it permits a bank holding company to control banks without any limitation on their activities, but provides that a bank holding company may control a "company which is not a bank" only if its activities are authorized under the closely related to banking or other nonbanking exceptions in the Act.[21]

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[19] Protestants suggest that Congress intentionally included a superfluous provision in order to establish a "catch-all" provision. The Board cannot accept this explanation, however, when the clear terms of the statute can be interpreted so as to give meaning to every word. *See Reiter* v. *Sonotone Corp.*, 442 U.S. 330, 339 (1979).

[20] 12 U.S.C. § 1841(d); *also see* 12 C.F.R. § 225.2(j).

[21] With respect to the Board's definition of "subsidiary" in Regulation Y, the regulation makes clear that the definition does not apply where the context otherwise requires. 12 C.F.R. § 225.2.

Protestants also point to the fact that the insurance provisions in section 4(c)(8) begin by using the term "bank holding company" but then state in Exemption D that this limitation applies also to a bank holding company *and* its subsidiaries. On this basis, protestants argue, the reference in section 4(a)(2) to activities engaged in by a "bank holding company" must also refer to activi-

B. *Prior Board Interpretations*

Since enactment of the BHC Act, the Board has not read the nonbanking prohibitions of section 4 as applying to the direct activities of holding company banks. On the contrary, the Board's actions and regulations over the years have consistently interpreted section 4 as *not* applying to such bank activities.[22] Protestants contend otherwise, pointing to section 225.21(a) of Regulation Y, which provides that "a bank holding company or a subsidiary may not engage in . . . any activity other than . . . an activity (permitted by section 4(c)(8))." The Board has never interpreted the provisions of Regulation Y relating to nonbanking activities as applicable to direct activities of banks, however.[23] For example, the Board

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ties conducted by its subsidiaries, banking and nonbanking alike. As noted, however, section 4(c)(8) sets forth an exemption to the general prohibition found in section 4(a) against a bank holding company owning shares of a nonbank company. Because this general prohibition does not apply to shares of a bank, section 4(c)(8) must necessarily apply only to nonbank companies. Thus, in context and consistent with the prohibition in section 4, the reference in the insurance provisions to subsidiaries must mean subsidiaries to which the prohibition applies.

[22] *See, e.g.*, 12 C.F.R. § 225.118(c); *American Bancorp, Inc.*, 39 *Federal Register* 22,468 (June 24, 1974); *Piedmont Carolina Financial Services, Inc.*, 59 Federal Reserve Bulletin 766, 767-68 (1973); *Cameron Financial Corp.* v. *Board of Governors*, 497 F.2d 841, 845 (4th Cir. 1974); *Board of Governors* v. *Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981); Fed. Res. Reg. Serv. 4-591 (Staff Op. January 12, 1982).

The Board notes that, contrary to protestants' implication, *Cameron* was not questioned by the Ninth Circuit ruling in *Patagonia Corp.* v. *Board of Governors*, 517 F.2d 803 (9th Cir. 1975), which distinguished *Cameron* and did not address the banking/nonbanking subsidiary issue. *See* 517 F.2d at 810-11 n.10.

[23] The original Regulation Y implementing the Act's provisions, adopted immediately after passage of the Act, contained no provision restricting the activities conducted directly by banks controlled by holding companies. 21 *Federal Register* 5686 (1956).

has never required bank holding companies that seek to acquire a bank to obtain prior approval under section 4(c)(8) for any nonbanking activities that might be engaged in directly by the bank, as would be required under protestants' construction of the statute. In addition, the section upon which protestants rely appears in a subpart of the Board's rules that pertains to the "*nonbanking* acquisitions and activities of bank holding companies." Thus, in context and consistent with the terms of section 4(a) of the Act, the reference in section 225.21 (a) of Regulation Y to subsidiaries means subsidiaries other than banks.[24]

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[24] Protestants cite several isolated phrases from various regulations to argue that the Board has "repeatedly affirmed that bank holding companies and *all* of their subsidiaries are subject to section 4." None of the examples cited, however, are persuasive. First, the Board's requirement that courier services not be conducted through a servicing arm of the bank (12 C.F.R. § 225.129) was imposed to eliminate possible unfair competition and supports the view that the Board has no authority to authorize activities for banks under the BHC Act.

Second, the Board's now-repealed interpretive rule on insurance services (12 C.F.R. § 225.128) referred to bank subsidiaries of bank holding companies because bank holding companies were authorized to sell credit insurance in connection with loans made by both their bank and nonbank subsidiaries.

Third, soon after enactment of the Act, the Board issued an opinion making clear that the exemption provided by section 4(c)(6) of the Act (providing that the section 4(a) prohibitions shall not apply to the acquisition of less than five percent of the voting shares of a nonbanking company) applies to shares held by banking subsidiaries of a bank holding company as well as shares held directly by the bank holding company itself. 12 C.F.R. § 225.101. This position is consistent with section 4(a)'s prohibition against the direct and indirect ownership or control of shares of a nonbanking company. It says nothing about the application of the activities limitation of section 4(a)(2).

Finally, with respect to the Board's regulation relating to investment company advisory activities (12 C.F.R. § 225.125), the Board has made clear that while that regulation did define bank holding company to include both bank and nonbank subsidiaries,

C. *Legislative History and Purposes of the Statute*

The Board's reading of the scope of the section 4(a) prohibitions is fully consistent with the Act's legislative history. When the nonbanking prohibitions in section 4 were adopted in 1956 as part of the original Act, Congress gave no indication that the statute was meant to affect in any way the activities engaged in directly by holding company subsidiary banks, whose powers traditionally were determined by the authority that issued the bank's charter.[25]

The 1970 amendment to section 4(c)(8) reinforced the view that section 4 does not reach the direct activities of banks controlled by holding companies. During proceedings on this amendment, Congress specifically considered and rejected a proposed amendment to section 4

"the restrictions contained in the interpretation on operations of banking subsidiaries were only intended to apply where the investment advisory function was being conducted by a nonbanking subsidiary of the bank holding company." Letter denying petition of Investment Company Institute, March 8, 1974.

[25] *See* S. Rep. No. 1095, Part 2, 84th Cong., 2d Sess. 5 (1956). The BHC Act does, however, provide the Board with certain supervisory authority over holding company banks. For example, the Board may examine any bank that is a subsidiary of a bank holding company (12 U.S.C. § 1844(c)) and is required to evaluate the management and financial condition of any bank that a bank holding company proposes to acquire (12 U.S.C. § 1842(c)).

Protestants argue that the Board's original *Merchants* decision is suspect because, according to protestants, the decision rested essentially on the premise that state banks are regulated exclusively by state law. Protestants have misread the Board's decision. As noted above, the Board recognizes that Congress intended for the OCC and the state banking authorities to remain as the *primary* (not exclusive) regulatory authorities responsible for their respective institutions. At the same time, the Board recognizes that the BHC Act provides the Board with certain supervisory authority over holding company banks. Second, the original decision, as well as the present one, rests on an interpretation of the explicit language of section 4 of the BHC Act.

that would have prohibited certain specified activities, including providing insurance, and that arguably applied to subsidiary banks as well as bank holding companies and their nonbank subsidiaries.[26]

There is also no indication that when in 1982 Congress incorporated the general prohibition on approving insurance activities into section 4(c)(8), Congress meant to expand the general nonbanking prohibitions in section 4(a). The relevant history instead indicates that Congress intended to retain the existing regulatory framework contained in section 4. The Board has found no legislative history expressly stating that the Garn-St Germain Act was intended to limit the direct insurance activities of holding company banks.[27] To the contrary, the Board

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[26] *See* 115 Cong. Rec. 33,133-34 (November 5, 1969); H.R. Rep. No. 387, 91st Cong., 1st Sess. 15 (1969); 115 Cong. Rec., E 9016-17 (daily ed. October 28, 1969) (statement of Rep. Brown); 115 *Cong. Rec.*, H 10503 (daily ed. November 4, 1969) (statement of Rep. Stanton). *Bills to Amend the Bank Holding Company Act of 1956; Hearings on S. 1052, S. 1211, S. 1664, S. 3823, and H.R. 6778 Before the Senate Comm. on Banking and Currency*, 91st Cong., 2nd Sess. 144, 157-158 (1970) (statement of Arthur Burns, Chairman of the Federal Reserve Board) (hereinafter cited as 1970 Senate hearings); 1970 Senate Hearings at 179-81 (Colloquy between Senator Packwood and Frank Wille, Chairman of the FDIC).

[27] The Board has considered protestants' references to language from the Senate Conference Report on Title VI of the Garn-St Germain Act (S. Rep. No. 97-641, 97th Cong. 2d Sess. 91 (1982), which states that Title VI would prohibit "bank holding companies and their subsidiaries" from selling and underwriting insurance. In the Board's view, in the context of the terms of the Act, the purpose of the Garn-St Germain Act, and the longstanding practice of not applying the nonbanking provisions of the Act to the direct activities of holding company banks, the reference in the report to subsidiaries was meant to refer to nonbanking subsidiaries.

The Board notes that references in earlier reports on the Title VI legislation indicate that section 4 and thus the proposed legislation would apply to bank holding companies and their "nonbank subsidiaries." S. Rep. No. 96-923, 96th Cong., 2d Sess. 2 (1980); S. Rep. No. 97-536, 97th Cong., 2d Sess. 36, 38-40 (1982). *See also,*

explicitly advised Congress during Congressional hearings in 1980 that the draft legislation (containing substantially the same language as ultimately enacted) would not limit the insurance activities of subsidiary banks. In response to a question concerning whether "a bank owned by a bank holding company [would] be allowed to sell automobile casualty or collision insurance" under the proposed bill, the Board stated that the answer would depend on the state or federal chartering authority.[28] It is clear from the legislative reports that the Garn-St Germain Act was intended to address certain Board decisions under section 4(c)(8) that allowed bank holding companies to sell credit related property and casualty insurance.[29] These Board decisions clearly did not authorize any activities for the subsidiary banks of the companies involved.

The Board believes that reading the Garn-St Germain Act as inapplicable to the direct insurance activities of banks does not frustrate the basic remedial purposes of the Act, which were to address what Congress believed to be potential unfair competitive practices associated with provision of insurance by banking organizations. In this regard, the Board notes that prior to 1982 insurance

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H.R. Rep. No. 96-845, 96th Cong., 2d Sess. 2-3 (1980) ("the BHC Act generally prohibits a bank holding company from owning the shares of any company that is not a bank.") There is no indication of any Congressional intent in the Title VI amendments to section 4(c)(8) of the Act to extend the coverage of the nonbanking prohibitions of section 4(a) of the Act to the direct activities of holding company banks.

[28] *Competition in Banking Act of 1980, Hearings Before the Senate Comm. on Banking, Housing and Urban Affairs*, 96th Cong., 2d Sess. 22 (1980).

[29] *See, e.g.*, S. Rep. No. 97-536, 97th Cong., 2d Sess. 36-37 (1982). The Board, of course, has no authority to authorize state or national banks to conduct nonbanking activities. That authorization must come from the state banking authorities or the Comptroller of the Currency, respectively.

activities conducted directly by banks were not extensive, since banks were authorized to engage in these activities only in a few states and the acquisition of banks by out of state bank holding companies was not permitted. In contrast, under the Board's section 4(c)(8) decisions, on which Congress specifically focused in enacting the Garn-St Germain Act, insurance activities could be conducted by nonbank companies in a holding company system on a nationwide basis.[30]

In any event, the Supreme Court has held that the purpose of legislation is determined in the first instance with reference to the plain language of the statute and that the broad purposes of legislation cannot be relied upon to overcome the terms of the statute itself.[31] As

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[30] After passage of the Garn-St Germain Act, in light of developments Congress could not necessarily have foreseen in 1982, the direct insurance activities of banks began to expand. The growth of interstate banking after the Supreme Court's decision in *Northeast Bancorp, Inc.* v. *Board of Governors*, 472 U.S. 159 (1985), resulted in the establishment by bank holding companies of interstate networks of banks that could sell insurance. During this period there also was a general expansion in the powers of banks. Since 1982, Congress has repeatedly considered proposed legislation that would restrain the direct insurance functions of banks on a permanent basis, but no such legislation has been enacted.

[31] *Board of Governors* v. *Dimension Financial Corporation*, 474 U.S. 361, 368, 373-374, (1986) ("If the statute is clear and unambiguous, 'that is the end of the matter, for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.'" (citations omitted)). *See also, Independent Insurance Agents of America, Inc.* v. *Board of Governors*, 835 F.2d 1452, 1456-1457 (D.C. Cir. 1987). As the Supreme Court recognized, the process of legislative compromise may result in the adoption of express exceptions that run counter to the general remedial purpose of the legislation. 474 U.S. at 374. The legislative history of the Garn-St. Germain Act reveals some disagreement among members of Congress as to whether banking organizations should be prohibited completely from engaging in insurance activities. 128 Cong. Rec. S 12,220-24, 12,230 (1982).

noted, in this instance, the terms of the BHC Act are clear that the direct activities of holding company banks are not restricted by section 4 of the Act.

Protestants argue that failing to interpret section 4's activities limitation to apply to banking subsidiaries of a bank holding company will permit states to "nullify the effect" of the Act by permitting state banks to engage in nonbanking activities that are forbidden by section 4. In establishing the BHC Act framework, however, Congress was required to draw the line between banking and nonbanking activities in the Act in some manner. As the terms of the Act demonstrate, Congress rationally did so on the basis of whether the entity conducting the activity is a bank or a nonbank.[32] Thus, where the company is chartered and operated as a bank under the definition in the BHC Act, it is outside the scope of the nonbanking provisions of the Act. But where the company is not a bank, it is, consistent with the line drawn by Congress in section 4, subject to the nonbanking provisions of the Act, and in order for these activities to be permissible, they must fit within one of the Act's authorizing provisions.

Protestants also rely on section 101(d) of CEBA, which amends section 3 of the BHC Act to permit qualified state-chartered savings banks to engage in any activity permitted by state law, but prohibits such savings banks from violating section 4(c)(8)'s insurance restrictions. 12 U.S.C. § 1842(f). Protestants assert that, if

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[32] Protestants point to several general references in the legislative history of the Act, as well as the 1966 and 1970 Amendments to the Act, to suggest that Congress intended to separate banking from nonbanking interests wherever the nonbanking interests were held, and that Congress intended for banks to divest themselves of their nonbanking interests. The Board agrees that one of the purposes of the BHC Act is to separate banking from commerce. As is evident in the terms and legislative history of the Act, Congress achieved this purpose by prohibiting banks from being affiliated within a bank holding company system with commercial companies.

section 4 did not restrict the nonbanking activities of banks, an exemption for savings bank would not have been necessary, nor would Congress have had any reason to apply the insurance restrictions uniquely to savings banks. Section 101(d), however, applies only to savings banks, which are not involved in this case, and does not extend the reach of section 4 of the BHC Act.

Moreover, it does not necessarily follow that this amendment to section 3 is an indication that Congress believed the restrictions in section 4 apply to all holding company banks. This amendment may have been intended merely to confirm, for this category of "banks," the Board's longstanding view that banks may engage in state-authorized activities in the face of contrary arguments advanced by insurance trade associations that the section 4 limitations apply to the direct activities of holding company banks. Congress' decision expressly to limit the insurance activities of these savings banks (in contrast to other types of holding company banks) is merely a part of a "special rule" adopted for those institutions under the BHC Act.[33] In fact, as noted, the 100th Congress actively considered (although it did not adopt) legislation expressly to extend these limitations to holding company banks—action that is inconsistent with protestants' interpretation of the Garn-St Germain Act.[34]

For the foregoing reasons, the Board has determined that section 4 of the BHC Act does not limit the sale of insurance directly by Anderson Bank and Mid State Bank within the banks as proposed, and that the banks may,

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[33] *See* H.R. Rep. No. 100-261, 100th Cong., 1st Sess. 130 (1987); S. Rep. No. 100-19, 100th Cong., 1st Sess. 33 (1987).

[34] Protestants' reliance on the nonbank bank provisions of CEBA also is misplaced. 12 U.S.C. § 1843(f). Such provisions were enacted in order to minimize the potential for unfair competition and adverse effects associated with the grandfather provisions applied to nonbank banks and their parent holding companies, not to expand the scope of the general prohibitions in section 4.

therefore, insofar as the BHC Act is concerned, resume within the banks the sale of insurance as permitted under Indiana law.[35]

IV. *Operating Subsidiaries of State Banks*

The Board emphasizes that its views regarding the coverage of section 4 in this Order pertain only where the activities are conducted directly by banks. The Order does not address the situation where the insurance activities are conducted by nonbank companies controlled by holding company banks. Under the Act, shares of a company held by a holding company bank are deemed to be indirectly held by the parent holding company (12 U.S.C. § 1841(g)) and, therefore, under the terms of the Act, their ownership or control by a bank holding company must qualify under the closely related to banking exception or one of the other exceptions in section 4 of the Act.[36]

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[35] Protestants request that the Board take cognizance of the public interest questions involved in the issue of whether section 4 applies to activities conducted directly by state banks. The Board is required by section 4(c)(8), in determining whether a particular activity is closely related to banking, to consider whether its performance by a bank holding company affiliate can reasonably be expected to produce public benefits that outweigh possible adverse effects. Because the Board has determined that section 4's prohibitions do not apply to activities conducted by Merchants' state bank subsidiaries, the Board need not decide whether these activities are closely related to banking or that their performance meets the net public benefits test of section 4(c)(8). The Board notes, however, that the insurance activities of the banks will be subject to the anti-tying restrictions of the 1970 Amendments to the BHC Act, which unlike section 4(a) explicitly apply to "banks." 12 U.S.C. § 1972(1).

[36] Similarly, a bank holding company is deemed to control any company that is controlled by the holding company's subsidiaries. 12 U.S.C. § 1841(a)(2). Under section 4(a)(2) of the Act, in order for the holding company to maintain control of such a company, the company must be a "bank" or a company whose activities

In this regard, in 1971 the Board adopted section 225.22 (d)(2) of Regulation Y (formerly section 225.4(e)), which authorizes a state bank owned by a bank holding company to acquire and retain all (but not less than all) of the voting shares of a company, without Board approval under the Act, so long as the company engages solely in activities the parent bank may conduct directly and at locations at which the bank could conduct the activities. 12 C.F.R. § 225.22(d)(2).[37] The Board adopted this regulation in order to permit holding company state banks to compete on equal footing with state banks that are not in a holding company system and in the absence of evidence that such acquisitions were resulting in evasions of the Act.[38] At that time, however, the Board stated that it would review the merits of the decision from time to time in light of its experience in administering the Act.[39]

In December 1988, in light of a number of developments, the Board asked for comment on whether to rescind

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qualify under one of the Act's nonbanking exceptions. 12 U.S.C. § 1843(a)(2).

[37] Section 225.22(d)(1) of Regulation Y authorizes a national bank to acquire and retain voting shares of a company in accordance with the rules of the Comptroller of the Currency. 12 C.F.R. § 225.22(d)(1).

[38] The regulation does not, as protestants assert, rest on the Board's "belief" that it has the authority to regulate the activities of subsidiary banks of bank holding companies.

[39] The Board stated:

> The Board should not at this time apply the [nonbanking] restrictions [of the BHC Act] to subsidiaries of banks. This decision is believed warranted by considerations of equity between banks that are and are not members of bank holding companies and by the absence of evidence that acquisition by holding company banks are resulting in evasions of the purpose of the Act. The merits of this decision will be reviewed by the Board from time to time in light of its experience in administering the Act. (36 *Federal Register* 9292 (May 22, 1971)).

this regulation, thereby requiring bank holding companies to obtain approval under section 4(c)(8) of the BHC Act prior to establishing or acquiring, through their subsidiary state banks, shares of companies engaged in activities that the bank is permitted to conduct under state law, unless the transaction is otherwise authorized under the Act. 53 *Federal Register* 48,915 (1988). The comment period on the proposal ends April 28, 1989.[40]

V. *Legislation Regarding Direct Activities of Holding Company Banks*

The Board notes that the 100th Congress had under active consideration legislation that would have applied the insurance prohibitions of the Garn-St Germain Act to the activities of holding company banks except where the bank was located in the same state as the bank holding company, the insurance activities were permissible under state law, and sales were limited to within the state. The insurance activities to be conducted by Merchants's subsidiary banks would not have been prohibited under these provisions. While this legislation was passed by the U.S. Senate and favorably reported by committees of the U.S. House of Representatives,[41] no legislation was enacted into

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[40] In December 1986, the Board asked for comment on whether to amend 12 C.F.R. § 225.22(d)(2) to prohibit bank holding companies from acquiring or retaining voting shares or control of companies engaged in real estate development activities or to limit such acquisitions to those situations that the Board proposed to permit for bank holding companies. 52 *Federal Register* 543, 551 (1987). The Board indicated that it would consider whether to apply the proposed restrictions to a wholly owned subsidiary of a holding company state bank. Contrary to protestants' implication, the proposed regulation would not bar state banks themselves that are owned by a holding company from engaging in state-authorized real estate activities within the bank.

[41] S. 1886, Title VIII, § 802, 100th Cong., 2d Sess., 134 Cong. Rec. S3437 (daily ed. March 30, 1988); H.R. 5094, Title III, § 302, 100th Cong., 2d Sess., 134 Cong. Rec. H6453 (daily ed. August 4, 1988), 134 Cong. Rec. H8470 (Sept. 27, 1988). *See also* S. Rep. No.

law. The Board calls to Merchants's attention, however, that subsequent Congressional action may modify the Board's Order granting Merchants's request for relief without providing so-called grandfather rights to continue the insurance activities. The Board retains jurisdiction over the application to act to carry out the requirements of any legislation adopted by Congress that would affect the conduct of insurance activities by Merchants's subsidiary banks under the BHC Act.

VI. *Request for a Hearing*

Protestants have requested that the Board grant discovery rights and conduct a hearing under section 5(f) of the Act (12 U.S.C. § 1844(f)) on the application in order to determine whether Merchants is attempting to evade the BHC Act, as forbidden by the *Citicorp (South Dakota)* decision. However, section 5(f) does not itself require that a hearing be conducted in any case; this section merely sets forth the powers the Board may exercise in any hearing or other proceeding undertaken under another provision of the Act.

Section 4(c)(8) does provide that in approving activities under that provision the Board must provide notice and opportunity for hearing. However, because the Board has determined that section 4 does not apply to the direct activities of Merchants's subsidiary state banks, the Board by this Order is not approving an application under section 4(c)(8). Accordingly, protestants do not have the right to a hearing or discovery in this case, and the Board does not believe such a proceeding would be appropriate under the facts and circumstances of this case.[42]

305, 100th Cong., 2d Sess., 108 (1988); H.R. Rep. No. 822 (Part 1), 100 Cong., 2d Sess., 166 (1988); H.R. Rep. No. 822 (Part 2), 100th Cong., 2d Sess., 80-81 (1988).

[42] Even where the applicable provision requires an opportunity for a hearing, such as under section 4(c)(8), a protestant is not entitled to discovery and a hearing on every application, but only

By order of the Board of Governors,[43] effective March 3, 1989.

/s/ Jennifer J. Johnson
JENNIFER J. JOHNSON
Associate Secretary of
the Board

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when there are material issues of fact in dispute. *Connecticut Bankers Assn.* v. *Board of Governors*, 627 F.2d 245 (D.C. Cir. 1980). In this case, there are no material issues of fact in dispute. Protestants present no specific allegations; rather, they assert that any evidence that might prove an evasive intent is in the hands of Merchants. Such a bare allegation is insufficient to show that material facts are in dispute. In any event, as noted above, the Board has determined that the factual basis for such evasion is not present in this case. Moreover, the Board retains supervisory authority to act under the BHC Act to prevent any evasion of the requirements of the Act or this order should that situation arise in the future.

[43] Voting for this action: Chairman Greenspan and Governors Johnson, Seger, Angell, Heller, Kelley, and LaWare.

APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, in the City of New York, on the 18th day of January, one thousand nine hundred and Ninety.

Docket Number 89-4030

INDEPENDENT INSUR AGNTS

v.

BD GOVS FRS

[Filed Jan. 18, 1990]

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the Petitioners, Independent Insurance Agents of America, Inc., Independent Insurance Agents of New York, Inc., New York State Assoc. of Life Underwriters and Professional Insurance Agents of New York, Inc.,

Upon consideration by the panel that heard the appeal, it is

Ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

/s/ Elaine B. Goldsmith
ELAINE B. GOLDSMITH
Clerk

APPENDIX E

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 559—August Term 1987

Argued: December 4, 1987 Decided: January 25, 1988

Docket No. 87-4118

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC.,
Petitioner,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent,

MERCHANTS NATIONAL CORPORATION, THE NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, THE NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, and THE NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, *Intervenors.*

Before:

NEWMAN, CARDAMONE, and PIERCE,
Circuit Judges.

Petition for review of an order of the Board of Governors of the Federal Reserve System approving an application by a bank holding company to permit two of its bank subsidiaries to engage in insurance activities, notwithstanding the moratorium imposed by Title II of the Competitive Equality Banking Act of 1987.

Petition granted and order vacated.

JONATHAN B. SALLET, Wash., D.C. (Jamie S. Gorelick, Jay L. Alexander, Miller, Cassidy, Larroca & Lewin, Wash., D.C., on the brief), *for petitioner and insurance-agent intervenors.*

RICHARD M. ASHTON, Assoc. Gen. Counsel, Wash., D.C. (Richard K. Willard, Asst. Atty. Gen., U.S. Dept. of Justice, Wash., D.C.; Michael Bradfield, Gen. Counsel, Douglas B. Jordan, Bd. of Governors of Fed. Reserve System, Wash., D.C., on the brief), *for respondent.*

JAMES A. MCDERMOTT, Indianapolis, Ind. (Stanley C. Fickle, Barnes & Thornburg, Indianapolis, Ind., on the brief) *for intervenor Merchants National Corporation.*

(Paul B. Galvania, Martin E. Lybecker, William L. Patton, Alan G. Priest, Mark P. Szpak, Ropes & Gray, Wash., D.C., filed a brief as amici curiae *for insurance company associations.*)

(John J. Gill, Gen. Counsel, Michael F. Crotty, Assoc. Gen. Counsel, American Bankers Assn., Wash., D.C., and Richard Whiting, Association of Bank Holding Companies, Wash., D.C., filed a brief as amici curiae *for American Bankers Association and Association of Bank Holding Companies.*)

(John L. Warden, H. Rodgin Cohen, Michael M. Wiseman, Lauretta E. Murdock, Charles S. Sullivan, Sullivan & Cromwell, New York, N.Y., filed a brief as amicus curiae *for New York Clearing House Association.*)

(Linley E. Pearson, Atty. Gen., J. Gordon Gibbs, Jr., Chief Counsel, Samuel L. Bolinger, Deputy Atty. Gen., Indianapolis, Ind., filed a brief as amicus curiae *for Indiana Dept. of Financial Institutions.*)

(James T. McIntyre, Jr., Leslie A. Dent, Hansell & Post, Wash., D.C., filed a brief as amicus curiae *for Insurance/Financial Affiliates of America, Inc.*)

(James F. Bell, Ernest Gellhorn, Carol R. Van Cleef, Imran M. Raschid, (Jones, Day, Reavis & Pogue, Wash., D.C., and Arthur E. Wilmarth, Jr., George Washington Univ. National Law Center, Wash., D.C., filed a brief as amicus curiae *for Conference of State Bank Supervisors.*)

JON O. NEWMAN, *Circuit Judge*:

The Independent Insurance Agents of America ("IIAA") petition for review of an order of the Board of Governors of the Federal Reserve System ("the Board" or "the Fed") permitting two Indiana state banks recently acquired by the Merchants National Corporation, a bank holding company, to resume specified insurance activities permitted under Indiana state law. The Board's approval rested upon a determination that the non-banking prohibitions of section 4 of the Bank Holding Company Act, as amended, 12 U.S.C. § 1843 (1982), do not apply to the insurance activities of the banking subsidiaries of bank holding companies. *Merchants National Corp.*, 73 Fed. Res. Bull. 876 (Sept. 10, 1987). For purposes of this appeal, the critical aspect of the Board's order is its conclusion that the order is not precluded by the moratorium Congress imposed upon federal banking agencies prohibiting for one year the approval of certain non-banking activities. The moratorium is contained in Title II of the Competitive Equality Banking Act of 1987 (CEBA), Pub. L. No. 100-86, §§ 201-205, 101 Stat. 552, 581-85 (1987) (to be codified at 12 U.S.C. § 1841 note). Section 201(b)(3) of the CEBA prohibits any federal banking agency from issuing, between March 6, 1987, and March 1, 1988, any rule, regulation, or order that would "have the effect of increasing the insurance powers" of any entity subject to the Bank Holding Company Act, and section 201(b)(4) specifically prohibits the Fed from approving the "acquisition" by a bank holding company of any entity, including a state-chartered bank, engaging in those insurance activities prohibited under sec-

tion 4 of the Bank Holding Company Act. We hold that the Board's *Merchants National* order is within the scope of the moratorium and therefore grant the petition for review and vacate the order.

The Statutory Framework

Before introducing the facts, it will be helpful to outline the pertinent statutory provisions of both the Bank Holding Company Act and the Competitive Equality Banking Act.

The Bank Holding Company Act of 1956. Though our disposition makes it unnecessary to rule on the Board's interpretation of section 4 of the Bank Holding Company Act, a brief mention of the Act's structure is appropriate as background. Briefly, the principal regulatory powers of the Fed under the Bank Holding Company Act are set forth in sections 3 and 4 of the Act. 12 U.S.C. §§ 1842, 1843. Section 3 requires Board approval of the acquisition of ownership or control of any bank by a bank holding company with narrow exceptions not here relevant.[1] Section 3 sets forth factors governing acquisition approval, focusing on the competitive effect of the proposed acquisition, the financial and managerial resources of both the holding company and the acquired bank, and the convenience and needs of the community served. 12 U.S.C § 1842(c).

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[1] Section 2 of the Act defines the term "bank holding company" in extensive detail, but for our purposes it may be understood simply as any company "which has control over any bank." 12 U.S.C. § 1841(a)(1). Until this year, a "bank" has been defined generally as any institution organized under state or federal law "which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans." 12 U.S.C. § 1241(c). Though not pertinent to the outcome of this appeal, it should be noted that this latter definition has been substantially amended by Title I of the Competitive Equality Banking Act of 1987, Pub. L. No. 100-86, § 101(a), 101 Stat. 552, 554.

Section 4 of the Act, the focal point of the Board's order in this case, regulates the non-banking activities of a bank holding company. Without intimating our views on the correctness of the Board's interpretation of the precise scope of section 4, it is sufficient to point out generally that section 4(a) prohibits a bank holding company from engaging in non-banking activities other than those permitted under section 4(c)(8) of the Act. Section 4(c)(8) sets forth the so-called "closely related to banking" exception to the non-banking provision. In relevant part, section 4(c)(8) states that the section 4(a) non-banking prohibitions shall not bar ownership by a bank holding company of:

> shares of any company the activities of which the Board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto, but for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to provide insurance as a principal, agent or broker . . .

12 U.S.C. § 1843(c)(8).

The Competitive Equality Banking Act of 1987. Title II of the CEBA[2] imposes a moratorium, effective between March 6, 1987, and March 1, 1988, on the exercise of federal banking agency authority relating to specified non-banking activities, including securities, real estate, and insurance activities of bank holding companies

[2] The other principal titles of the 1987 Act, among other things, amend the definition of the term "bank" as used in the Bank Holding Company Act (Title I), provide recapitalization for the Federal Savings and Loan Insurance Corporation (Title III), establish in the Federal Deposit Insurance Corporation emergency authority over failing banks (Title IV), clarify the role of the National Credit Union Administration (Title V), and set forth regulations relating to the practices of depository institutions delaying the availability of deposited funds (Title VI).

or their subsidiaries in order that Congress may have the opportunity to "conduct a comprehensive review of our banking and financial laws and to make decisions on the need for financial restructuring legislation in the light of today's changing financial environment . . . before the expiration of such moratorium." CEBA, § 203 (a).

That part of the moratorium statute relating to insurance activities of bank holding companies and their subsidiaries is divided into two primary substantive subsections. Section 201(b)(3) of Title II states:

> A Federal banking agency *may not issue any* rule, regulation, or *order that would have the effect of increasing the insurance powers of* banks, *bank holding companies*, foreign banks or other companies subject to the Bank Holding Company Act of 1956 under section 8(a) of the International Banking Act of 1978, *or banking* or nonbanking *subsidiaries thereof* with respect to any activities in the United States, either with respect to specific banks or bank holding companies or subsidiaries thereof or generally beyond those expressly authorized for bank holding companies under subparagraphs (A) through (G) of section 4(c)(8) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(c)(8)(A) through (G)).

(Emphasis added).

Section 201(b)(4) contains the second moratorium provision relating to insurance, and specifically concerns the Fed. This provision states that during the moratorium period the Board

> *may not approve the acquisition by a bank holding company* or by a foreign bank or other company subject to the Bank Holding Company Act of 1956 under section 8(a) of the International Banking Act of 1978, *of* any company, including *a State-chartered*

> *bank, unless the bank holding company*, foreign bank, or other company *has agreed to limit the insurance activities in the United States of the company to be acquired to those permissible under section 4(c)(8)* of the Bank Holding Company Act of 1956.

(Emphasis added). Finally, section 202 of Title II states that nothing in the section 201 moratorium provisions is intended to prevent a regulated agency from issuing any rule, regulation, or order pursuant to preexisting legal authority "to expand the securities, insurance, or real estate powers of banks or bank holding companies . . . if the effective date of such rule, regulation, or order is delayed until the expiration" of the moratorium period, March 1, 1988.

The Facts

A number of states, including Indiana,[3] historically have authorized state-chartered banks to provide insurance services to their customers. On July 1, 1986, Merchants National Corporation, a bank holding company within the meaning of the Bank Holding Company Act, 12 U.S.C. § 1841(a), sought permission from the Fed to acquire the stock of two banks chartered under the laws of the State of Indiana, the Anderson Banking Company ("Anderson Bank") and the Mid State Bank of Hendricks County ("Mid State Bank"). Both of these state banks had engaged in general insurance activities prior to the date of Merchants National's applications, Anderson Bank directly since its incorporation in 1916, and Mid State Bank since its purchase of an insurance agency in 1985.[4]

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[3] Ind. Code § 28-1-11-2 provides: "Any bank or trust company shall have power . . . to solicit and write insurance as agent or broker for any insurance company authorized to do business in this state, other than a life insurance company."

[4] Merchants National subsequently made a commitment that Mid State Bank would transfer to itself all insurance activities from its insurance agency subsidiary and thereafter conduct all such activities directly in the bank.

The initial Merchants National applications were protested by various insurance industry trade groups, including the IIAA, on the ground that the provisions of section 4 of the Bank Holding Company Act apply to the insurance activities of state banks owned by bank holding companies and therefore that the acquisitions of Anderson Bank and Mid State Bank could not be approved without requiring termination of their insurance activities to the extent required under section 4. In response to the protests, Merchants National committed that it would cause the banks to divest their insurance agency activities within two years unless, within that time, it received Board approval for the banks to retain their insurance activities. Merchants National agreed that, prior to such approval, the banks would limit their insurance activities to the renewal of existing policies. In light of these commitments, the Board approved the applications on October 29, 1986. 72 Fed. Res. Bull. 838 (1986).

On February 5, 1987, Merchants National filed an application seeking Board approval for Anderson Bank and Mid State Bank to resume the insurance activities that had just been suspended pursuant to the acquisition commitments. Merchants National sought permission on two alternative grounds. First, it contended that Anderson Bank and Mid State Bank were exempt from the insurance provisions of section 4 of the Bank Holding Company Act pursuant to the "grandfather" provisions of section 4(c)(8)(D), as amended, under which a bank holding company or any of its subsidiaries is permitted to engage in insurance agency activity in which the holding company or the subsidiary was engaged on May 1, 1982, subject to certain geographical and functional limitations. Second, Merchants National sought more broadly a determination that the non-banking prohibitions of section 4 of the Act do not apply to activities conducted directly by banking subsidiaries of a bank holding company.

After giving interested parties an opportunity to comment, *see* 52 Fed. Reg. 8966, 8967 (March 20, 1987), the

Board on September 10, 1987, issued the order challenged on this appeal, permitting the two Indiana banks to resume their insurance activities. The Board ruled first that the grandfather provision in section 4(c)(8)(D) of the Bank Holding Company Act was inapplicable because that provision insulates only those entities that were bank holding companies or their subsidiaries as of May 1, 1982. Neither Anderson Bank nor Mid State Bank qualified under this provision. However, the Board agreed with Merchants' alternative contention that the section 4 prohibitions did not apply to the insurance activities of banking subsidiaries of bank holding companies.

The Board made its September 10, 1987, order effective immediately. In doing so, the Board determined that the moratorium contained in the CEBA did not apply to its approval of Merchants National's application because the action neither "increas[ed] the insurance powers" of Merchants National or its banking subsidiaries in contravention of section 201(b)(3), nor "approve[d] the acquisition" of a bank in contravention of section 201(b)(4). On October 6, 1987, this Court entered a stay of the Board's order pending review.

Discussion

Our analysis begins and ends with consideration of the moratorium issue because we hold that the issuance of the Merchants National order violates the CEBA moratorium.

In construing the moratorium, we recognize the admonition of the Supreme Court that where a statute is "silent or ambiguous" with respect to a specific issue, a court should defer to the construction adopted by the agency administering the statute whenever the agency has adopted a "permissible construction of the statute." *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984) (footnote omitted). At the same time we also recognize that *Chevron* enjoins

courts to "give effect to the unambiguously expressed intent of Congress." *Id.* Though the classification of congressional intent as clear or ambiguous will sometimes be in the eye of the beholder, courts construing statutes enacted specifically to prohibit agency action ought to be especially careful not to allow dubious arguments advanced by the agency in behalf of its proffered construction to thwart congressional intent expressed with reasonable clarity, under the guise of deferring to agency expertise on matters of minimal ambiguity. *See Greater New York Hospital Ass'n v. Blum,* 634 F.2d 668, 673 (2d Cir. 1980) (agency view of statute more persuasive on issue that does not concern agency's jurisdiction). Congress enacted the CEBA moratorium to stop federal banking agencies from taking certain actions for a one-year interval so that Congress itself could have the opportunity to decide how to resolve certain controversies in the banking field. An enactment of that sort must not be given a crabbed interpretation that risks undermining its purpose.

Before examining in detail the two pertinent provisions of the moratorium, it is important to view them together in order to appreciate the evident purpose of Congress. Section 201(b)(4) prohibits the Board from approving a bank holding company's acquisition of a bank unless the acquired bank has agreed to limit its insurance activities to those permitted under section 4(c)(8) of the Bank Holding Company Act. Section 201(b)(3) prohibits any banking agency, including the Board, from issuing any order that has the effect of increasing the insurance powers of a bank holding company or its subsidiary banks. The combined effect of these two provisions is evident: no new insurance activities by bank holding companies or their bank subsidiaries during the moratorium by means of either acquisition of a bank already selling insurance or approval for a previously acquired bank to sell insurance. With this structure of the moratorium in mind, we turn to the Board's efforts to interpret each of

the moratorium provisions to permit the Merchants National order.

With respect to section 201(b)(4), the Board does not deny that this moratorium provision contemplates precisely the situation presented by the Merchants National application in all but one respect. Though section 201(b)(4) requires the Board to withhold approval of those activities specifically sought to be engaged in by the two bank subsidiaries of Merchants National, the Board points out that section 201(b)(4) applies only to Board approval of *acquisitions* of such banks so engaged. The Board's position is that because the state bank "acquisitions" were approved in 1986, before the beginning of the moratorium, approval of the subsequent application to resume suspended insurance activities is not subject to the terms of section 201(b)(4).

As applied to the circumstances of Merchants National's acquisitions of the Anderson and Mid State banks, we find the Board's reading of section 201(b)(4) untenable. The acquisitions, approved October 29, 1986, were conditioned upon a commitment by the holding company that the acquired state banks would cease their insurance activities within two years and severely curtail those activities in the interim. These commitments were understood to be necessary "in order to expedite Board approval for the acquisition of the banks," Brief of Respondent at 39. Though it is true that Merchants National's "acquisitions" were approved in a technical sense before the beginning of the moratorium, the reality is that the technique of granting acquisition approval subject to a commitment effectively split each acquisition into two parts, with the second aspect, the commitment, covering the rights to engage in insurance activities. This latter and, for present purposes, critical bundle of rights was not acquired until the commitment was lifted by the September 10, 1987, order under review, and that action was taken during the moratorium.

While we do not criticize the creative approach to expediting approval in this case, such creativity may not be used to thwart the congressional will by splitting an "acquisition" and thus evading the purpose of section 201(b)(4). It is particularly noteworthy that the commitments by Merchants National effectively to cease its acquired banks' insurance activities, which facilitated Board approval of the expedited acquisitions, are the very same conditions that section 201(b)(4) requires to make permissible an acquisition during the moratorium period that would otherwise be impermissible.[5] The Board's present order completes the acquisitions by lifting conditions during a time when the moratorium requires those conditions to be imposed. We find the irony too much to bear and conclude that the Board's construction of the statutory language would permit an evasion of its purpose under the circumstances of this case.

Even were we to agree with the Board's reading of section 201(b)(4), we would in any event hold that its order is plainly covered by section 201(b)(3) of the moratorium. The Board contends that section 201(b)(3) does not apply because the order does not "increas[e] the insurance powers" of either Merchants National or the two Indiana subsidiary banks. The reason for this, argues the Board, is that the term "powers" is used in

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[5] Section 201(b)(4) states that the moratorium imposed by its terms shall not apply:

> to the acquisition of a State-chartered bank by a bank holding company that on March 6, 1987, controlled one or more State-chartered banks that have engaged in insurance activities identical to those of the newly acquired institution so long as the bank holding company agrees that it will—
>
> (A) within 2 years of the consummation of its acquisition of the State-chartered bank, divest or terminate that bank's impermissible insurance activities, and
>
> (B) limit the bank's insurance activities during that 2 year period to the renewal of existing policies.

section 201(b)(3) in some technical or legal sense and that the ban on agency actions "increasing the insurance powers" of a regulated bank refers only to changes made in the bank's organic charter by the chartering authority. The Board supports this novel reading of the unmodified word "powers" by relying on its determination that under section 4 of the Bank Holding Company Act it has no authority to regulate the insurance activities of a state bank subsidiary, and concludes that its order is outside the scope of the "insurance powers" moratorium because Anderson Bank and Mid State Bank "already have these powers by virtue of state law and those powers are not and have never been limited by the [Bank Holding Company] Act." Order at 17, 73 Fed. Res. Bull. at 881.

This reading of the statute does not withstand scrutiny. To begin with, there is nothing in the statute to suggest that Congress intended only some technical meaning by its use of the word "powers." In fact, the phrase Congress used imposes a moratorium on agency action "that would have the *effect* of increasing the insurance powers," CEBA, § 201(b)(3) (emphasis added), suggesting a broad reading that gives the term "powers" a nontechnical, functional meaning. Indeed, upon analysis the Board's reasoning is circular. The argument is that the moratorium applies only to insurance powers increased pursuant to the Board's legal authority, and because the Board believes it has no legal authority over state bank subsidiaries of bank holding companies under section 4 of the Bank Holding Company Act, the moratorium does not apply to its Merchants National order. The fault lies in the middle premise. Whatever the merits of the Board's view that section 4 excludes from the scope of its insurance prohibitions all bank subsidiaries of bank holding companies, the fact remains that the moratorium was enacted in part so that Congress could resolve precisely that issue. The insurance moratorium was imposed in

part due to disagreement over the nature and extent *under existing law* of those regulatory "powers" referred to by section 201(b)(3). Congress gave itself until March 1, 1988, to resolve this question free from agency action, and the Board may not ignore the congressional command on the ground that in its view the answer is clear. The scope of section 201(b)(3) must be left sufficiently capacious to include those agency actions bearing on matters withdrawn by Congress during the term of the moratorium.

The legislative history of the moratorium supports this understanding of those agency actions subject to its terms. One of the substantive issues Congress hoped to consider during the moratorium period is the so-called "South Dakota loophole."[6] As the Senate Report explains:

> Section 4(c)(8) [of the Bank Holding Company Act], as amended in 1982 by the Garn-St. Germain Act, limits the insurance activities of bank holding companies. The scope of those limitations is in dispute. All parties agree that the limitations apply to a bank holding company and its nonbank subsidiaries. Insurance industry groups contend that the limitations also apply to every bank controlled by a bank holding company, whereas bank holding companies contend that the limitations do not apply to banks. Pursuant to the latter argument, a major bank holding company sought to conduct insurance activities beyond those permissible under section 4(c)(8) through a State-chartered bank in South Dakota. Although that application [w]as denied, the

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[6] The phrase refers to a controversial South Dakota statute permitting a bank holding company to acquire a state bank for the purpose of engaging in insurance activities through the state bank. *See Citicorp/South Dakota*, 71 Fed. Res. Bull. 798 (1985).

> so-called "South Dakota loophole" remains a source of controversy.

S. Rep. No. 19, 100th Cong., 1st Sess. 16, *reprinted in* 1987 U.S. Code Cong. & Admin. News 489, 506. *See also id.* at 44; H. Rep. No. 261, 100th Cong., 1st Sess. 148, *reprinted in* 1987 U.S. Code Cong. & Admin. News 588, 617. Though this discussion mentions the issue in the context of the acquisition provision of the moratorium, section 201(b)(4), rather than the increased powers provision, section 201(b)(3), it is clear from this legislative history that the Board's authority to regulate the insurance powers of state chartered banking subsidiaries of bank holding companies under current law was a matter of controversy in the first session of the 100th Congress, and this very controversy in part motivated passage of the moratorium. Whether Congress ultimately agrees or disagrees with the Board's interpretation of section 4 of the Bank Holding Company Act remains to be seen. But in light of the congressional intent to freeze agency action bearing on the contested issue until March 1, 1988, it would undermine the purpose of the moratorium to give it an artificially restricted interpretation, especially one that rests on a resolution of an issue that Congress has temporarily reserved for its own consideration.

Nor do we find persuasive the Board's reliance on section 201(d) and 201(e)(2) of the moratorium, which provide, respectively, that nothing in Title II shall "be construed to increase or reduce the insurance authority of bank holding companies or banking or nonbanking subsidiaries thereof or of national banks under current law" and that "neither the existence of the moratorium nor its expiration shall be construed to increase, decrease, or affect in any way the authority of State-chartered bank subsidiaries of bank holding companies with respect to insurance activities." These provisions

mean only that neither the fact of the moratorium's passage nor its terms should be understood to change existing laws as it relates to the "South Dakota loophole" debate.[7] To rely on sections 201(d) and 201(e)(2) in interpreting the moratorium as if this debate never took place is to strip the moratorium's substantive provisions of all force, at least as they relate to state bank subsidiaries. In short, these provisions do not limit the scope of the moratorium itself.

There remains the question of relief. The Board, relying on section 202 of the CEBA, contends that even if the moratorium is applicable, "the order would not be invalid and the most IIAA would be entitled to is a stay of the order's effective date until the moratorium expires." Brief of Respondent at 47. We disagree. Section 202 permits an agency to issue rulings otherwise subject to the moratorium "if the effective date of such rule, regulation, or order is delayed until the expiration of such moratorium." The Board, however, did not delay the effective date of the Merchants National order, and we decline the invitation to amend the Board's order in order to preserve its validity. It should be unnecessary to remind the Board that the courts must not substitute their own judgment for that of the agency on matters of agency discretion. *See SEC v. Chenery Corp.*, 332 U.S. 194 (1947). We have no authority to predict that the Board, now advised that the moratorium applies to the approval of Merchants National's application, will choose to reissue its order with an effective date of March 1, 1988. The proper course is to vacate the order and permit the Board to proceed as it sees fit in a manner consistent with our decision and applicable law.

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[7] *See* 133 Cong. Rec. S3936 (daily ed. Mar. 26, 1987) (colloquy between Sen. Breaux and Sen. Proxmire); *id.* at S3939 (colloquy between Sen. Riegle and Sen. Proxmire); *id.* at S3957 (colloquy between Sen. Dodd and Sen. Proxmire).

In view of our disposition, it is both unnecessary and inappropriate for us to review that portion of the Board's order that concerns the scope of the non-banking prohibitions of section 4 of the Bank Holding Company Act.

The petition for review is granted, and the order of the Board is vacated.

Supreme Court, U.S.
FILED
MAY 17 1990
JOSEPH F. SPANIOL, JR.
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No. 89-1620

In the Supreme Court of the United States

OCTOBER TERM, 1989

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., and THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

Petitioners,

v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM and MERCHANTS NATIONAL CORPORATION,

Respondents.

On Petition For Writ Of Certiorari
To The United States Court of Appeals
For The Second Circuit

BRIEF IN OPPOSITION OF RESPONDENT MERCHANTS NATIONAL CORPORATION

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QUESTION PRESENTED

Whether § 4 of the Bank Holding Company Act prohibits a bank owned by a holding company from engaging in activities authorized for banks by the bank's chartering authority.

RULE 29.1 LISTING

Merchants National Corporation has no parent company or any non-wholly owned subsidiaries.

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In the Supreme Court of the United States

OCTOBER TERM, 1989

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., and THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

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STATEMENT

The order of the respondent Board of Governors of the Federal Reserve System ("Board") at issue grants an application by Merchants National Corporation ("Merchants"). (Pet. App. 22a-45a). In the proceeding to review the Board's order brought by the petitioners Independent Insurance Agents of America, Inc., et al. ("Insurance Agents"), Merchants was granted leave to intervene by the Court of Appeals for the

Second Circuit ("Second Circuit") and appeared as intervenor to argue that the petition for review should be denied. As intervenor below, Merchants is automatically a party to the proceedings in this Court. Sup. Ct. R. 12.4. Merchants submits this brief in opposition to the Insurance Agents' petition for a writ of certiorari to review the Second Circuit's decision.[1]

REASONS FOR DENYING THE WRIT

The Petition claims (1) that § 4 of the Bank Holding Company Act of 1956, as amended, 12 U.S.C. § 1843, precludes a state-chartered bank owned by a bank holding company from engaging in insurance agency activities authorized for banks by the bank's chartering authority, and (2) that the decision below presents some major issue regarding the proper methodology for judicial review of administrative agency interpretations of federal statutes. The Petition is wrong.

As this Court has taken pains to explain, the first and only task on judicial review is to give effect to the "unambiguously expressed intent of Congress" where that intent is discernible on the face of the statute. *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984). Only if the statute is ambiguous or silent on the issue need the court go further and inquire if the agency's "construction" is a "permissible" one. 467 U.S. at 843.

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[1] Although labelled "Intervenor" in the caption of the Petition for Certiorari, Merchants should have been named a "Respondent" and properly appears as such before this Court. *Id.*; *see* R. STERN, E. GRESSMAN & S. SHAPIRO, SUPREME COURT PRACTICE 344, 348-49 (6th ed. 1986).

In this case, the Second Circuit upheld the Board's construction of § 4 as permissible on the premise that the words of the statute did not specifically resolve the issue presented. That decision is clearly correct if the premise is assumed. In fact, however, there was no need to proceed to the second stage of the inquiry under *Chevron*. The plain and unambiguous words of § 4 affirmatively establish that it does not regulate the activities of subsidiary banks. Both that section and the structure of the entire Act clearly show that the Board has no statutory authority to prevent a holding company's acquisition of a bank based on the activities in which the bank is engaged.

The Second Circuit's decision thus upholds a Board order that comports with and is compelled by the explicit terms of the statute. The decision is correct, conforms with prior decisions of this Court, does not conflict with any decision of any other federal court, and does not warrant further review.

I. *BOTH THE PLAIN LANGUAGE OF § 4 AND THE STRUCTURE OF THE ENTIRE ACT SHOW THAT § 4 DOES NOT REGULATE THE ACTIVITIES OF BANKS.*

The Bank Holding Company Act was adopted against the background of Congress' historic commitment to the dual banking system in this Nation. Under that system, national banks are chartered pursuant to, and their powers defined by, the National Bank Act, 12 U.S.C. §§ 1 *et seq*. State banks, by contrast, are chartered under and their powers defined by state statutes and regulations. The "primary supervisor" of national banks with plenary authority to govern their activities is the Comptroller of the Currency, not the Board. The primary super-

visors of state banks are state officials and agencies acting under state law.[2]

In enacting the Bank Holding Company Act and giving the Board supervisory authority over bank *holding companies*, Congress did not alter this dual banking system or the allocation of supervisory authority over *banks* and *banking activity*. "Underlying the [Bank Holding Company Act] as a whole" were the "broad[] purposes" to "retain local, community-based control over banking." *Northeast Bancorp, Inc. v. Board of Governors*, 472 U.S. 159, 172 (1985). The Act therefore does not purport to define the powers of banks or to regulate banking activities according to a uniform federal standard of what banks "ought to do."

Rather, the Bank Holding Company Act begins by distinguishing between a "bank holding company" on the one hand, and a "bank" on the other. 12 U.S.C. § 1841(a)-(c). Section 3 of the Act then sets forth the terms and conditions under which a bank holding company may acquire and control a bank. 12 U.S.C. § 1842. Section 3(c) specifies in detail the factors the Board must consider in passing on an acquisition application. None permits the Board to deny an application based upon the powers the bank itself is authorized to exercise pursuant to its charter under state or federal law. *See* 12 U.S.C. § 1842(c).

Section 4 of the Act, by contrast, does not regulate a holding company's acquisition and control of banks. Rather, § 4 ad-

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[2]Even with respect to state banks insured by the Federal Deposit Insurance Corporation ("FDIC"), the Board is the primary federal regulator for *that* purpose only of those banks which are members of the Federal Reserve System; for the vast majority of insured state banks, the primary federal regulator is the FDIC. *See* Scott, *The Dual Banking System: A Model of Competition in Regulation*, 30 STAN. L. REV. 1, 3-7 (1977).

dresses a bank holding company's ownership and control of *non*banking subsidiaries and its engagement in activities *other than* owning and managing banks. Although § 4 is lengthy, its plain language makes clear that it imposes *no* restriction on the kinds of banks that a holding company may own. The section provides in pertinent part:

> § 1843. Interests in nonbanking organizations.
>
> Ownership or control of voting shares of any company not a bank; engagement in activities other than banking.
>
> (a) Except as otherwise provided in this chapter, no bank holding company shall --
>
> (1) . . . acquire direct or indirect ownership or control of any voting shares of any company which is not a bank, or
>
> (2) . . . retain direct or indirect ownership or control of any voting shares of any company which is not a bank or bank holding company or engage in any activities other than (A) those of banking or of managing or controlling banks and other subsidiaries authorized under this chapter or of furnishing services to or performing services for its subsidiaries, and (B) those permitted under paragraph (8) of subsection (c) of this section . . . .
>
> Exemptions
>
> (c) The prohibitions in this section shall not . . . apply to --
>
> . . . .
>
> (8) shares of any company the activities of which the Board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto, but for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to pro-

> vide insurance as a principal, agent, or broker except [as stated in (A) through (F) and subsequent proviso] . . . .

12 U.S.C. § 1843(a),(c).

As that plain language shows, the only prohibitions in § 4 are stated in subsection (a). The entirety of subsection (c), including (c)(8) upon which the Insurance Agents rely, is devoted to listing *exemptions* to the prohibitions otherwise stated in subsection (a). Subsection (c)(8) itself generally permits the Board to *allow* otherwise prohibited ownership of *non*bank companies if it determines that their activities are "so closely related to banking or managing or controlling banks as to be a proper incident thereto . . . ." The subsequent "insurance" limitations in subsection (c)(8) are not independent "prohibitions" but rather are *limitations on the exemption* -- *i.e.*, limitations on the Board's authority to *expand* the permissible scope of bank holding company activity in areas "closely related to banking or managing or controlling banks . . . ."[3]

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[3]This meaning of § 4(c)(8) is confirmed by a careful parsing of the statutory language. Section 4(c) generally provides that "*[t]he prohibitions* in *this section* shall *not . . . apply* to -- . . ." (emphasis added). "[T]his section" is § 4. "The prohibitions" in "this section" are not stated in § 4(c) -- rather, they are set forth in § 4(a). Subsection 4(c) states a variety of "exemptions" to those § 4(a) prohibitions, including the several exemptions set forth in (c)(1) through (c)(14). The exemption stated in subsection (c)(8), like each of (c)(1) through (c)(14), applies to the "shares of any company . . . ." Those "compan[ies]," to which "[t]he prohibitions in this section shall not . . . apply", can only be the *non*bank companies whose shares a holding company would otherwise be prohibited by § 4(a) from owning or controlling -- *i.e.*, in the words of § 4(a)(1)-(2), "any company which *is not a bank*" (emphasis added). Similarly, the provision in § 4(c)(8) that insurance activities are not "closely related to banking" is express-

Footnote continued on next page

The exercise of Board authority to expand the scope of permissible holding company activity -- *i.e.*, to create an exemption from § 4(a)'s prohibitions -- is not the issue in this case. Rather, the question presented here is whether holding companies are prohibited from owning or controlling banks that engage in activities permitted by the bank's chartering authority. That question turns *solely* on the terms of subsection (a), and that subsection contains no such prohibition.

To the contrary, careful examination of subsection (a) reveals three -- and only three -- prohibitions:

First, "no bank holding company shall -- (1) . . . *acquire* direct or indirect ownership or control of any voting shares of any company *which is not a bank* . . . ." 12 U.S.C. § 1843(a)(1) (emphasis added).

Second, "no bank holding company shall . . . (2) . . . *retain* direct or indirect ownership or control of any voting shares of any company *which is not a bank* or bank holding company . . . ." 12 U.S.C. § 1843(a)(2) (emphasis added).

Third, "no bank holding company shall . . . (2) . . . *engage in any activities* other than (A) those of *banking or of managing or controlling banks* and other subsidiaries authorized under this chapter . . . *and* (B) those permitted under [§ 4(c)(8)]." *Id.* (emphasis added). This third prohibition directly parallels the first two in relevant part. The first two prohibitions *do* permit a holding company to acquire and retain control of *banks* and the third explicitly permits the holding company to "engage in" the activity of "managing or controlling" those same banks.

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ly limited to the Board's *exemption* authority under § 4(c)(8) -- *i.e.*, in the words of the statute, "for purposes of *this subsection* . . ." 12 U.S.C. § 1843(c)(8) (emphasis added).

A holding company necessarily engages in the activity of "managing or controlling banks" when it manages or controls entities that are "banks" as defined by the Act.[4] Neither § 4(a) nor any other provision of the Act goes beyond the minimum statutory definition of a "bank" to define what constitutes *the business of "banking"*. Only a bank's *chartering authority* defines the business of "banking" -- it does so by enumerating the authorized powers and activities of banks. Nothing in § 4 (or any other section of the Act) provides otherwise.

Thus, the plain language of § 4(a)(2)(A) is dispositive of the issue in this case. That subsection permits a holding company, independent of and unmodified by *any* limitation or condition, to engage in the activity of "managing and controlling banks".

The Insurance Agents suggest that a bank holding company is "engaged" in whatever activity its subsidiaries are engaged, including its bank as well as its nonbank subsidiaries. (*See* Pet. 15). No provision of the statute so states and, indeed, § 4 is carefully drafted to avoid that result. Section 4(a) *distinguishes* between a bank holding company's "acquir[ing]" and "retain[ing] *direct or indirect* ownership or control . . . of any company which is not a bank" on the one hand, and the holding company's own "engag[ing]" in "activities" on the other. The

[4]Under the Act and subject to certain exceptions, an entity is a "bank" if it is either "[a]n insured bank as defined in section 3(h) of the Federal Deposit Insurance Act" or "[a]n institution organized under the laws of the United States, any State of the United States [or various U.S. territories] which both - (i) accepts demand deposits or deposits that the depositor may withdraw by check or similar means . . .; and (ii) is engaged in the business of making commercial loans." 12 U.S.C. § 1841(c). As this Court has held, the Board has *no* authority to revise the Act's definition of a "bank". *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361 (1986).

"direct or indirect" provisions modify *only* a holding company's prohibited acquisition and retention of *ownership of a nonbank*; they prevent holding companies from acquiring or retaining control of nonbanks directly or through one or more (otherwise exempted) nonbank subsidiaries. There is *no* "direct or indirect" provision modifying the "activity" in which a holding company itself may "engage", as one would expect from the context had Congress intended the "engage[ment in] activities" prohibition to include the activities of its subsidiaries.

More generally, the Insurance Agents' purported construction of § 4's term "engage" gives no content to and would read out of the statute any distinction between (1) a holding company's acquisition and retention of nonbanks and (2) a holding company's engagement in activities. It would make § 4's structure futile and wholly unnecessary. Under the Insurance Agents' theory that a holding company "engages" in whatever activity its subsidiaries, bank as well as nonbank, engage, all Congress had to do was provide that "no bank holding company shall engage, directly or indirectly, in activities other than" some prescribed list of activities in which Congress wanted bank holding companies and their subsidiaries to engage. That is not the statute Congress enacted.

The Insurance Agents also say that a holding company cannot own a bank subsidiary which engages in an activity not permitted by § 4(c)(8) because that subsection is "incorporated by reference into Section 4(a)(2)". (Pet. 15). In fact, § 4(c)(8) is *not* "incorporated" into § 4(a)(2)(A) -- which authorizes a holding company to engage in the activity of "managing or controlling banks". The latter provision is unqualified and disposes of this case. When § 4(a)(2) refers to § 4(c)(8) activities, it explicitly provides that the permissible activities for

holding companies include *both* "(A) banking or . . . managing or controlling banks . . ., *and* (B) [the activities] permitted under [subsection (c)(8)]." 12 U.S.C. § 1843(a)(2) (emphasis added).

The statute does not say that the activities in which a holding company is permitted to "engage" are "those of managing or controlling banks *but only to the extent allowed*" -- or "only as permitted" -- by subsection (c)(8). Indeed, such statutory language, and therefore the Insurance Agents' purported "construction", would not even make sense. The activities "permitted under" subsection (c)(8) are *not* those which constitute "banking or managing or controlling banks," but rather are *additional* activities that the Board determines are "*closely related*" to "banking or managing or controlling banks". In making that "closely related" determination, the Board must necessarily look to other laws to define what activities *are* "banking" because the Bank Holding Company Act does not. The Board's reference must be to the law under which banks are organized and their permissible powers and activities defined, that is, the chartering authorities of the banks themselves.[5]

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[5]Section 4(a)(2)'s "incorporation" of § 4(c)(8) -- *i.e.*, the cross reference to § 4(c)(8) in § 4(a)(2)(B), *not* § 4(a)(2)(A) -- parallels for the holding company's own operations the § 4(c)(8) exemption for its nonbank subsidiaries. Where the Board determines that a particular activity is "closely related" to banking or managing or controlling banks, § 4(c)(8) allows the holding company to own nonbank subsidiaries engaged in that activity and § 4(a)(2)(B) "permit[s]" the holding company to engage in the same "activit[y]" directly. Subsections 4(a)(2)(A) and 4(c)(1) reflect a similar parallelism. *Compare* 12 U.S.C. § 1843(a)(1)(A) *with* 12 U.S.C. § 1843(c)(1)(C).

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In sum, the "insurance" restrictions in § 4(c)(8) are -- and are only -- restrictions on the Board's authority to grant exemptions to the prohibitions imposed by § 4(a) in the first place. Section 4(a) imposes *no* prohibition on a holding company's ownership of a *bank* of any kind, including one engaged in insurance activities. Furthermore, § 4(a)(2)(A) explicitly authorizes a holding company to "engage" in the "activity" of "managing or controlling banks" unmodified by *any* restriction or condition. It makes no grammatical sense and does violence to the plain meaning of the statutory language to contend that the insurance limitations on the § 4(c)(8) exemption constitute restrictions on *bank* activities.

Although the Insurance Agents and their political allies have repeatedly urged Congress to enact legislation regulating the activities of banks owned by holding companies, "[t]he short answer is that Congress did not write the statute that way". *United States v. Naftalin*, 441 U.S. 768, 773 (1979). The Insurance Agents' efforts to have the courts create a statutory prohibition, based on quite selective views of the "purposes" of the Act, such as "separat[ing] the banking industry from general commercial activities" unmodified by context (Pet. 6), should be summarily dismissed. As this Court only recently held under this Act:

These provisions further demonstrate Congress' determination to distinguish between the activities of (1) a bank; (2) a bank holding company; and (3) a holding company's nonbank subsidiary. Such parallel provisions, stating separately the activities in which a holding company may "engage" and the character of the nonbank subsidiaries it may own (based upon their engagement in the same activities), would be completely unnecessary if a holding company were deemed to "engage" in those activities in which its subsidiaries engage.

> The "plain purpose" of legislation . . . *is determined in the first instance with reference to the plain language of the statute itself*. . . . Application of "broad purposes" of legislation at the expense of specific provisions ignores the complexity of the problems Congress is called upon to address and the dynamics of legislative action. Congress may be unanimous in its intent to stamp out some vague social or economic evil; however, because its members may differ sharply on the means ofor effectuating that intent, the final language of the legislation may reflect hard-fought compromises. Invocation of the "plain purpose" of legislation at the expense of the terms of the statute itself takes no account of the processes of compromise and, in the end, prevents the effectuation of congressional intent.
>
> . . . .
>
> If the Banking Holding Company Act falls short of providing safeguards desirable or necessary to protect the public interest, that is a problem for Congress, and not the Board or the courts, to address.

Board of Governors v. Dimension Financial Corp., 474 U.S. 361, 373-74 (1986) (emphasis added; citations omitted).[6]

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[6]It is particularly silly to suggest that judicial re-writing of the Bank Holding Company Act is necessary to prohibit abusive "tying" arrangements. (Pet. at 7, 10-11). Another federal statute, 12 U.S.C. §§ 1971 *et seq.*, directly prohibits such activities, a prohibition enforceable by civil penalities imposed by the applicable banking supervisor, injunctive actions by the Attorney General, and private actions for treble damages and attorney fees. 12 U.S.C. §§ 1972(2)(F)(i), 1973, 1975. Further, that statute, which (1) traces to the same 1970 legislation that amended the Bank Holding Company Act and (2) explicitly applies to

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II. *THE PLAIN MEANING OF § 4 IS CONFIRMED BY THE PURPOSES OF THE ACT.*

The bulk of the Insurance Agents' Petition has little to do with the actual language of § 4 but rather advances "policy" considerations based on the supposed "purposes" of the Bank Holding Company Act. (*See generally*, Pet. 8-12, 15-17). Properly considered, the statutory purposes do not conflict with but rather confirm the scope and limits of the prohibitions established by § 4(a).

When the Bank Holding Company Act was enacted in 1956, banks and the activities in which they could engage were already extensively regulated by the laws under which the banks were organized -- state laws in the case of state-chartered banks and federal law in the case of banks chartered under the National Bank Act. However, the development of bank holding companies had created a means by which a bank's parent company and the parent's non-bank subsidiaries could engage in many types of unrelated activity free of regulation. The Bank Holding Company Act was passed for the explicit purpose of limiting those *unregulated* holding company activities which *inter alia* permitted the circumvention of state banking law and regulation. *See* H. R. Rep. No. 609, 84th Cong., 1st Sess., at 2-4 (1955); S. Rep. No. 1095, 84th Cong., 1st Sess., at 2 (1955).

A purpose to regulate or prohibit these unregulated activities of holding companies does not imply a further purpose to regulate or prohibit the already regulated activities of subsidiary banks. As even the Insurance Agents must recognize, Congress' focus was on the holding company itself -- an entity

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"*banks*" as well as bank holding companies, shows that Congress knew perfectly well how to write legislation to regulate the activities of subsidiary banks when it wished to do so.

which otherwise could, through its ownership of a bank, "*combine* banking and non-banking activities within a single corporate structure." (Pet. 6; emphasis aded). The "congressional policy" underlying § 4 was to prevent "control of banking and nonbanking *enterprises* by a single business entity." *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980) (emphasis added).

That policy is not implicated when, as here, a *bank* owned by a holding company engages in activities *authorized for banks* by the bank's chartering authority and primary supervisor. In that circumstance, the involvement of the holding company does *not* create any "combination of activities" that would not otherwise be present. In terms of the facts of this case, the two state banks involved already engaged in insurance agency activities -- and did so under longstanding Indiana law -- before they were acquired by Merchants.

Thus, the scope and limits of § 4 established by the plain statutory language -- *i.e.*, prohibiting and regulating activities by holding companies and their nonbank subsidiaries, but specifically authorizing holding companies to manage and control banks, with no restrictions on their ability to do so -- conforms precisely with the congressional purpose. Congress implemented its policy against "combination of activities" by filling the perceived gap in the regulatory structure. It regulated the formerly unregulated entity (the holding company and its nonbank subsidiaries); it had no need to and did not go further and impose additional regulation on the already-regulated subsidiary banks.[7]

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[7]Although the Insurance Agents imply that this leaves the Bank Holding Company Act open to evasion by "intracorporate maneuvering" (Pet. 6), they identify no way in which this can actually occur. State and federal banking laws regulate the activities in which the banks may engage, and the Bank Holding Company Act regulates those in

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By contrast, the Insurance Agents' contrary "construction" of § 4 would result in a major reallocation of supervisory responsibility over banks and a drastic expansion of federal regulation to the detriment of state law. As the Insurance Agents recognize (Pet. 9), the jurisdictional issue of the Board's authority does not merely involve insurance agency activities authorized for banks but many others as well. Under their view

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which the holding company and its other, nonbank subsidiaries may engage. Neither matter is within the control of the holding company.

Moreover, the Act repeatedly draws distinctions based on the corporate forms. For example, § 5 of the Act, 12 U.S.C. § 1844, gives the Board authority to order a holding company or its *nonbank* subsidiaries to terminate activities in certain circumstances. In those same circumstances, the Board is also authorized to require divestiture by the holding company of ownership or control of an offending *nonbank* subsidiary. However, no authority is given to the Board to order a *bank* subsidiary to terminate any activity, regardless of the potential risk entailed; nor is any authority given to require divestiture of a bank subsidiary in any circumstance. *See* 12 U.S.C. § 1844(e)(1). *See also, e.g., Cameron Financial Corp. v. Board of Governors*, 497 F.2d 841 (1974) (application of § 4(a)'s grandfather clause depends upon whether a bank or a nonbank subsidiary was conducting the activity before the effective date).

The Insurance Agents also say the Board is inconsistent in interpreting the § 4(a) prohibitions to apply to the nonbank subsidiaries of banks. (Pet. 5, 17). No issue regarding nonbank subsidiaries of banks is presented in this case and, as the Second Circuit noted, resolution of that issue of the Board's authority is properly left to a case which presents it. (Pet. App. 15a). In any event, the Board's recent reversal on the issue of nonbank subsidiaries of banks -- *see, e.g.*, Pet. App. 42a-43a (discussing former Regulation Y); *American Bancorp, Inc.*, 39 Fed. Reg. 22468 (1974); *Piedmont Carolina Financial Services, Inc.*, 59 Fed. Res. Bull. 766, 767-68 (1973) -- provides no legal basis for overriding the plain statutory language in the case of banks themselves.

of § 4, the Board, rather than the Comptroller in the case of national banks and state law and regulatory agencies in the case of state banks, would determine the activities in which banks may engage in the guise of making § 4(c)(8) "exemption" decisions.[8]

Such a drastic expansion of federal law to the detriment of the States is not lightly presumed, and should never be assumed absent clear statutory language showing that was Congress' intention. Doing so would be particularly inappropriate in this case. The pertinent provisions of § 4(a) were enacted over *40 years ago*, they have *never* been amended in any relevant respect, and the Board has *never* construed that language as giving it regulatory authority over the activities of banks. (*See* Pet. App. 33a-34a). Thus, for example, the Board's regulation implementing the § 4(c)(1) exemption for nonbank subsidiaries, 12 U.S.C. § 1843(c)(1), provides that:

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[8]No reading of § 4 could restrict this expansion of Board authority to the "insurance" limitations contained in § 4(c)(8), and the Insurance Agents do not pretend otherwise. If banks owned by holding companies were limited to activities the Board determines are "closely related" to banking under § 4(c)(8), that limitation would necessarily extend to any and all areas of bank powers and activities.

The Court should not underestimate the magnitude of the expansion of federal law this would entail. Information presented by the Indiana Department of Financial Institutions to the Second Circuit showed that of 237 banks chartered under Indiana law, 179 were owned by a holding company. *Brief Of The Indiana Department Of Financial Institutions As Amicus Curiae In Support Of Respondent* at 4, Second Circuit No. 89-4030. Thus, with respect to over 79% of the state banks in Indiana, the law governing and regulatory authority over a presently indeterminable number of bank activities would pass from State into Federal hands.

> The Board has ruled heretofore that the term "services" as used in section 4(c)(1) is to be read as relating to those services . . . which a bank itself can provide for its customers . . . . *A determination as to whether a particular service may legitimately be rendered or performed by a bank for its customers must be made in the light of the applicable Federal or State statutory or regulatory provisions. In the case of a State-chartered bank, the laws of the State in which the bank operates, together with any interpretations thereunder rendered by appropriate bank authorities, would govern the right of the bank to provide a particular service.* In the case of a national bank, a similar determination would require reference to provisions of Federal law relating to the establishment and operation of national banks, as well as to pertinent rulings or interpretations promulgated thereunder.

12 C.F.R. § 225.118(c) (1990) (emphasis added). This regulation, which interprets the scope of § 4 of the Act in the relevant respect, was promulgated in 1964. *See id.* Congress has never acted to overrule it.

The Insurance Agents' purported "construction" of § 4 is not supported by the authority to prevent "evasions" of the Act claimed by the Board in *Citicorp (South Dakota)*, 71 Fed. Res. Bull. 789 (1985). (Pet. 17). The Board asserted authority in that case under § 5 of the Act. 71 Fed. Res. Bull. at 790 n.3. After this Court's decision in *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361 (1986), the Board authority asserted in *Citicorp* is in serious question. (*See* Pet. App. 8a n.2). But in any event, whether or not the Board has the authority under § 5 it claimed in *Citicorp*, that would not show that the Board has authority under § 4 to regulate the activities

of banks; and the plain language of the statute shows the opposite.[9]

Finally, the Insurance Agents' position is not supported by their misleading characterization of *Board of Governors v. Investment Company Institute ("ICI")*, 450 U.S. 46 (1981). To the contrary, that case refutes their position. *ICI* involved a Board regulation under § 4(c)(8)'s "closely related to banking" exemption that allowed a holding company (or a nonbank subsidiary) to act as an organizer, sponsor and investment advisor for a closed-end investment company. In upholding the regulation, this Court rejected the claim that the Board's regulation would impermissibly allow *banks* owned by holding com-

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[9]Furthermore, the facts of this case are not remotely similar to those in *Citicorp*. The state statute in that case, enacted in 1984, permitted an out-of-state holding company to acquire a single South Dakota bank. It simultaneously placed severe restrictions on such a bank's engagement in both banking and insurance activities within South Dakota. 71 Fed. Res. Bull. at 789. Thus, the Board could infer that the purpose of that statute and Citicorp's proposed acquisition thereunder was to allow a bank holding company to evade the purposes of the Act by permitting it to engage in an out-of-state insurance business. *Id.* at 790.

Here, by contrast, the Indiana legislature long ago determined it to be in the public interest for Indiana banks to compete in the area of insurance agency activities other than life insurance. IND. CODE § 28-1-11-2 (1988). This statutory authorization traces to the Financial Institutions Act of 1933, and that enactment confirmed bank practices under prior Indiana law. The Anderson Banking Company, for example, has engaged in such insurance activities since its incorporation in 1916. (Pet. App. 67a-68a n.2). This state law authorization applies to all Indiana-chartered banks, and it long preceded the Bank Holding Company Act of 1956. Accordingly, its "purpose" was *not* to create some peculiar new form of "bank" permitting a holding company to evade the restrictions imposed by federal law.

panies to engage in that activity. The Court held that "*the Board does not have the power to confer such authorization on banks*," and then quoted with approval the Board's interpretation of its authority under the Act:

> The authority of national banks or state member banks to furnish investment advisory services does not derive from the Board's regulation; *such authority would exist independently of the Board's regulation and its scope is to be determined by a particular bank's primary supervisory agency.*

450 U.S. at 59 n.25 (emphasis added). Thus, this Court recognized (1) that § 4(c)(8) applies only to holding companies and their nonbank subsidiaries, *not* to banks; and (2) that the authorized activities of banks exist independently of the Act and derive from their chartering authorities.

Confronted with that holding in *ICI*, the Insurance Agents say that the Court's footnote "goes on to uphold" restrictions on banks that prevented holding companies from evading the Act and that this "sort of evasion is exactly what is at issue here." (Pet. 18 n.10). In fact, the "restrictions" imposed by the Board's ruling did *not* restrict banks from engaging in their *own* investment advisory activities if and as permitted by their chartering authority.

Rather, the Board's regulation and interpretative ruling, which permitted holding companies (and their nonbank subsidiaries) to engage in such activities, at the same time placed certain restrictions on the manner in which that activity could be conducted. The restrictions on banks to which the Insurance Agents refer simply prohibited banks from performing certain subsidiary functions to assist or promote the *holding company's* investment advisory activity in ways similar to those prohibited

to the holding company itself.[10] As this Court noted, those restrictions applied "to banks *when the investment advisory function was performed by a holding company or its nonbanking subsidiary*" in order to prevent "evasion" of the similar restrictions placed on those entities. 450 U.S. at 60 n.25 (emphasis added). There were no restrictions on banks performing investment advisory functions themselves (or upon the manner in which they conducted those activities), the authority for which "would exist independently of the Board's regulation and its scope [would be] . . . determined by a particular bank's primary supervisory agency." *Id.* at 59 n.25.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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[10]For example, the holding company could not "engage directly or indirectly, in the sale . . . of securities of any investment company for which it acts as investment advisor." 450 U.S. at 53 n.13. Therefore, the subsidiary bank employees could not "express . . . opinion[s] with respect to the advisability of purchase of securities of any investment company for which the *holding company* acts as advisor." *Id.* (emphasis added).

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No. 89-1620

In the Supreme Court of the United States

OCTOBER TERM, 1990

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., ET AL., PETITIONERS

v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE FEDERAL RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the Board of Governors of the Federal Reserve System properly concluded that Section 4 of the Bank Holding Company Act of 1956, 12 U.S.C. 1843, does not restrict bank subsidiaries of a bank holding company from selling insurance as authorized by state law.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-19a) is reported at 890 F.2d 1275. The order of the Board of Governors of the Federal Reserve System (Pet. App. 22a-45a) is reported at 75 Fed. Res. Bull. 388.

JURISDICTION

The judgment of the court of appeals was entered on November 29, 1989. A petition for rehearing was denied on January 18, 1990. Pet. App. 46a. The petition for a writ of certiorari was filed on April 18, 1990. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Under the Bank Holding Company Act of 1956, 12 U.S.C. 1841 *et seq.*, the Board of Governors of the Federal Reserve System regulates the acquisition of state and national banks by bank holding companies, *i.e.*, any company that has direct or indirect control of any bank, 12 U.S.C. 1841(a). Section 4 of the Act, 12 U.S.C 1843, imposes certain ownership and operational restrictions on bank holding companies. With respect to ownership restrictions, Section 4(a)(1) and (2) of the Act, 12 U.S.C. 1843(a)(1) and (2), provides that no bank holding company shall directly or indirectly acquire or retain control of "any company which is not a bank." With respect to operational restrictions, Section 4(a)(2) of the Act, 12 U.S.C. 1843(a)(2), prohibits a bank holding company from "engag[ing] in any activities other than (A) those of banking or of managing or controlling banks and other subsidiaries authorized under [the Act] * * *, and (B) those permitted under [Section 4(c)(8) of the Act, 12 U.S C. 1843(c)(8)]."

Section 4(c)(8) of the Act, 12 U.S.C. 1843(c)(8), provides that the "nonbanking" restrictions imposed in Section 4(a) "shall not, with respect to any * * * bank holding company, apply to * * * any company the activities of which the Board * * * has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto * * *." Section 4(c)(8), however, expressly provides that "for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to provide insurance as a principal, agent, or broker," subject to certain exceptions not relevant here. 12 U.S.C. 1843(c)(8).

2. In July 1986, respondent Merchants National Corporation, a bank holding company headquartered in Indianapolis, sought the Board's permission to acquire two

Indiana-chartered banks, the Mid State Bank of Hendricks County and the Anderson Banking Company. Pet. App. 53a. Each of those state banks engaged in insurance agency activities permitted under Indiana law. See Ind. Code Ann. § 28-1-11-2 (Burns 1986).[1] Petitioners, various insurance industry trade associations, protested Merchants' applications, contending that Merchants' ownership and operation of bank subsidiaries that sold insurance would violate Section 4(c)(8) of the Act, 12 U.S.C. 1843(c)(8). In response to those protests, Merchants told the Board that,

> unless it received Board approval in the meantime for the banks to retain their insurance activities, it would cause the banks to divest the insurance agency activities within two years and, in the interim, to refrain from the sale of insurance except for the renewal of existing policies.

Pet. App. 23a-24a. In light of those commitments, the Board approved Merchants' applications to acquire the two state banks in October 1986. *Id.* at 6a-7a, 23a, 68a.

In February 1987, Merchants asked the Board to permit its two Indiana-chartered banks to resume the insurance activities that had been suspended under its acquisition commitments. Pet. App. 54a. Petitioners renewed their protests against such activities. In September 1987, the Board granted Merchants' request. *Id.* at 67a-82a. The Board concluded

> that the direct insurance activities of Anderson and Mid State Banks are not limited by the nonbanking provi-

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[1] Anderson Bank has engaged directly in insurance agency activities since the bank's incorporation in 1916. Mid State Bank acquired an insurance agency in 1985. Pet. App. 22a-23a. As part of the acquisition proposal before the Board, Mid State Bank agreed to "transfer the insurance activities of the subsidiary to the bank itself, which will thereafter conduct the activities directly." *Id.* at 23a n.1.

> sions of section 4 of the [Bank Holding Company] Act * * * [because those provisions] do not apply to limit the *direct* activities of holding company banks * * *.

Id. at 71a.[2] Moreover, in rejecting petitioners' construction of the Act, the Board noted that it "has not * * * since enactment of the Act read [12 U.S.C. 1843(a)(2)] or any other portion of the nonbanking prohibitions of section 4 as applying to the direct activities of holding company banks." Pet. App. 73a. And the Board determined that its application of Section 4 was consistent with the legislative history and structure of the Act. *Id.* at 73a-76a. Finally, the Board concluded that the Competitive Equality Banking Act of 1987 (CEBA), Pub. L. No. 100-86, Tit. II, §§ 201-205, 101 Stat. 581-585, which prohibited federal banking agencies from approving certain nonbanking activities for a period of one year, did not preclude its order. Pet. App. 79a-81a.

On the insurance industry trade associations' petition for review, the court of appeals in January 1988 granted the petition and vacated the Board's order. Pet. App. 47a-63a. The court held that the CEBA moratorium, which ran from March 6, 1987, until March 1, 1988, barred the Board's order. *Id.* at 55a-62a.[3] Accordingly, the court vacated the Board's order and remanded the case for further proceedings. Given that disposition, the court found "it [was] both unnecessary and inappropriate * * * to review that por-

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[2] The Board rejected Merchants' alternative contention that relief should be granted under the grandfather provision of Section 4(c)(8)(D) of the Act, 12 U.S.C. 1843(c)(8)(D), which generally permitted a bank holding company to engage in any insurance activity in which the bank holding company or subsidiary was engaged in on May 1, 1982. The Board found that Anderson Bank was not a subsidiary of a bank holding company on that date and that Mid State Bank did not begin selling insurance before that date. Pet. App. 70a-71a.

[3] The CEBA moratorium expired on March 1, 1988, without renewal.

tion of the Board's order that concerns the scope of the nonbanking prohibitions of section 4 of the Bank Holding Company Act." *Id.* at 63a.

3. In light of the scheduled expiration of the CEBA moratorium, Merchants again asked the Board to permit its two Indiana-chartered banks to resume the insurance activities that had been suspended under its acquisition commitments. As a result, petitioners renewed their protests. In March 1989, the Board reaffirmed its earlier order granting Merchants' request. Pet. App. 22a-45a.[4]

In concluding that "the nonbanking provisions of section 4 do not limit the *direct* activities of holding company banks," Pet. App. 27a-28a, the Board first considered the express terms and structure of the Bank Holding Company Act. The Board noted that "[t]he language of the activities limitation in section 4(a)(2) forbids 'bank holding companies'—not 'banks'—from engaging in activities other than those specified in that provision." Pet. App. 30a. The Board pointed out that the Act

> defines "bank holding company" to mean any company that has control over any bank, a definition that clearly refers only to the parent holding company itself, not to the system as a whole or to any "subsidiary," a term that is separately defined.

Ibid. (footnotes omitted).

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[4] The Board again rejected Merchants' alternative contention that relief should be granted under the grandfather provision of Section 4(c)(8)(D) of the Act, 12 U.S.C. 1843(c)(8)(D). Pet. App. 26a-27a; see note 2, *supra*. The court of appeals did not disturb that aspect of the Board's order, see Pet. App. 9a n.3. That contention is no longer at issue.

The Board also rejected petitioners' request to grant discovery rights and conduct a hearing on Merchants' application. Pet. App. 44a. Petitioners sought no further review of that aspect of the Board's order.

Moreover, the Board determined that

> [t]he structure of the * * * Act indicates that this provision of section 4(a)(2) * * * was intended to apply to the activities of bank holding companies themselves, many of which are operating companies engaged directly in nonbanking activities as well as in controlling banks and companies engaged in permissible nonbanking activities.

Pet. App. 30a. In this regard, the Board noted that Section 4(a) "distinguishes between a bank holding company's acquiring and retaining 'direct or indirect' ownership or control of any company that is not a bank, on the one hand, and the holding company's engaging in activities itself, on the other." Pet. App. 31a. By contrast, the Board observed, "[i]n the activities limitation of section 4(a)(2), * * * Congress did not use the words 'directly or indirectly' to modify the word 'engage.' " *Ibid.* The Board thus concluded that this difference confirms "Congress' intent to apply the activities limitation in section 4(a)(2) to the holding company only and not to its subsidiaries." *Ibid.*

Second, the Board stated that "[s]ince enactment of the [Bank Holding Company] Act, [it] has not read the nonbanking prohibitions of section 4 as applying to the direct activities of holding company banks." Pet. App. 33a. To the contrary, the Board reiterated that its "actions and regulations over the years have consistently interpreted section 4 as *not* applying to such bank activities." *Ibid.*

Third, the Board determined that its "reading of the scope of the section 4(a) prohibitions is fully consistent with the Act's legislative history." Pet. App. 35a. In this regard, the Board noted that the "1970 amendment to section 4(c)(8) reinforced the view that section 4 does not reach the direct activities of banks controlled by holding companies," *ibid.*, and that there was "no indication that when in 1982 Con-

gress incorporated the general prohibition on approving insurance activities into section 4(c)(8), Congress meant to expand the general nonbanking prohibitions in section 4(a)," *id.* at 36a.[5]

4. In November 1989, the court of appeals denied the insurance industry trade associations' petition for review. Pet. App. 1a-19a. In light of petitioners' challenge to the Board's construction of Section 4 of the Bank Holding Company Act, 12 U.S.C. 1843, the court stated that its

> task is to determine whether Congress has "directly spoken to the precise question at issue," and, if so, to give effect to any "unambiguously expressed intent of Congress," or, if not, to determine "whether the agency's answer is based on a permissible construction of the statute."

Pet. App. 11a (quoting *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-843 (1984)). Turning first to the terms of the statute, the court "[could] not say that the provisions of the Act reveal an unambiguous congressional intent concerning the precise question at issue." Pet. App. 11a. Consequently, the court considered

> whether the Board's interpretation of the language that does appear in the Act is reasonable, an inquiry we

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[5] The Board noted that Congress had recently considered, but did not enact, various bills

> that would have applied the insurance prohibitions of [Section 4(c)(8)] to the activities of holding company banks except where the bank was located in the same state as the bank holding company, the insurance activities were permissible under state law, and sales were limited to within the state.

Pet. App. 43a. The Board therefore "call[ed] to Merchants's [*sic*] attention * * * that subsequent Congressional action may modify the Board's Order granting Merchants's [*sic*] request for relief without providing so-called grandfather rights to continue the insurance activities." *Id.* at 44a.

> undertake by examining all relevant sources, including such clues as the statutory language may provide.

Id. at 12a.

The court found unpersuasive the Board's textual arguments that "the limitations of section 4(a)(2) apply in terms to 'bank holding companies,' not to 'banks,' " Pet. App. 12a, and that "because the 'ownership clause' of section 4(a)(2) does not bar a bank holding company from owning subsidiary banks, the 'activities clause' should be interpreted not to apply to activities of subsidiary banks," *ibid.* Similarly, the court found wanting petitioners' assumption that the statutory bar against bank holding companies from engaging in nonbank activities "means 'engage in directly or through subsidiaries.' " *Ibid.*

On the other hand, the court found "[s]omewhat more supportive of the Board's position * * * textual arguments arising from comparisons of the 'activities clause' with other language in section 4(a)(2)." Pet. App. 12a. First, the court noted that Section 4(a)(2)'s "grandfather proviso" uses the phrase "in which directly or through a subsidiary," and that the "ownership clause" speaks of "direct or indirect" ownership of nonbanks, and "no similar phrase modifies the prohibition on engaging in nonbank activities." *Id.* at 12a-13a. The court thus observed that "[t]he use of these phrases in section 4(a)(2) and their absence from the 'activities clause' might imply a deliberate congressional choice not to restrict the activities of bank subsidiaries * * *." *Id.* at 13a.[6]

The court also determined that the "Board derives a somewhat stronger argument for its interpretation from the

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[6] The court went on to note, however, that those differences in language "might also result from drafting different clauses at different times and assembling them without intending differences in phrasing to have significance." Pet. App. 13a.

structure of the Act." Pet. App. 13a. The court took account of the Board's conclusion

> that if the "activities clause" applied to subsidiaries of a bank holding company, the "ownership clause" would be virtually superfluous, since, under that reading, the "activities clause" alone would preclude a bank holding company from owning a nonbank.

Ibid. On the other hand, the court noted that petitioners found "support for [their] interpretation in the structure of section 4 * * * [in that] subsidiary banks [may be] subject to the 'activities clause' because they are within the category of entities exempted from that clause by section 4(c)(8)." *Id.* at 14a.[7]

Turning to the legislative history of the Act, the court stated that various remarks in the *Congressional Record* "do not provide unambiguous support for [petitioners'] interpretation." Pet. App. 16a. The court also found that the legislative history as a whole was "remarkably free of clear statements indicating disapproval of nonbanking activities engaged in directly by bank subsidiaries." *Ibid.* Indeed, the court pointed out that during the relevant committee hearings, "the attention of Congress was specifically called to the range of activities that state chartering authorities were permitting for bank subsidiaries of bank holding companies, * * * and some Congressmen expressed the view that the

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[7] The court appeared to take issue with

> the Board's contention that though it has no authority to preclude bank subsidiaries of a bank holding company from engaging in nonbank activities, it does have authority to preclude the subsidiaries of a bank subsidiary from engaging in nonbank activities.

Pet. App. 14a. Nonetheless, since this case did not involve such "subsidiaries of a bank subsidiary," the court chose "not to resolve the issue of the Board's authority over the nonbank activities of subsidiaries of bank subsidiaries until that issue is squarely presented." *Id.* at 15a.

holding company bill would not modify such state regulatory authority." *Id.* at 16a-17a.[8]

"After assessing all of the relevant considerations," the court concluded, it was

> satisfied that the Board, acting within its sphere of competence, has made a reasonable interpretation of section 4(a)(2), one that confides decisions concerning the scope of insurance and other nonbank activities of bank subsidiaries to their national and state chartering authorities.

Pet. App. 19a.[9]

ARGUMENT

1. Petitioners contend (Pet. 12-15) that the court of appeals' decision misapplied the principles of *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), requiring courts to defer to an agency's reasonable interpretation of a statute Congress has entrusted it to administer. In particular, petitioners claim that the court of appeals erroneously upheld the Board's order "[w]ithout study of the express statutory language and congressional purpose." Pet. 13.

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[8] The court also observed that "[s]ubsequent legislative forays into the field, though an uncertain source of prior congressional intent at best, * * * reveal primarily that Congress finds this is a difficult area in which to provide clear answers." Pet. App. 17a.

[9] The court recognized that "[i]f that interpretation is to be altered, Congress will have to enact suitable legislation." Pet. App. 19a.

The court of appeals dissolved the previously imposed stay pending appeal once it denied the petition for rehearing. Pet. App. 46a. On February 2, 1990, Justice Stevens, sitting as Circuit Justice, denied petitioners' application to stay the court of appeals' mandate pending the filing and disposition of the petition for a writ of certiorari. See Pet. 6 n.3.

The court of appeals, however, did not depart from the established *Chevron* framework. As this Court has made clear, the first stage of the *Chevron* framework requires a reviewing court to determine "whether Congress has directly spoken to the precise question at issue." *Chevron*, 467 U.S. at 842. This question must be answered by "employing traditional tools of statutory construction." *Id.* at 843 n.9; see *Fort Stewart Schools* v. *FLRA*, 110 S. Ct. 2043, 2046 (1990). Here, the court of appeals "look[ed] to the particular statutory language at issue as well as the language and design of the statute as a whole." *K Mart Corp.* v. *Cartier, Inc.*, 486 U.S. 281, 291 (1988). First, the court considered various provisions of the Bank Holding Company Act and found that none "reveal[ed] an unambiguous congressional intent concerning the precise question at issue." Pet. App. 11a; see *id.* at 12a-13a. Second, the court looked to the "structure" of the Act and again determined that it alone did not resolve the issue. *Id.* at 13a-15a. Third, the court reviewed the pertinent legislative history of the Act, together with "[s]ubsequent legislative forays into the field," *id.* at 17a, and concluded that such materials did not clarify the otherwise ambiguous statutory language. *Id.* at 16a-19a.

The court of appeals therefore determined that "Congress has [not] directly spoken to the precise question at issue," *Chevron*, 467 U.S. at 842, only after analyzing the Act's language, structure, and legislative history. Having done so, the court properly proceeded to the second stage of the *Chevron* framework – determining whether the agency has adopted a reasonable interpretation of an otherwise ambiguous statute. See Pet. App. 12a ("The question * * * is whether the Board's interpretation of the language that does appear in the Act is reasonable.").[10] Here, the court again

[10] Petitioners' criticism of the court of appeals' application of the *Chevron* framework is nothing more than a dispute about the organiza-

considered the Act's language, structure, and legislative history and concluded that "the Board, acting within its sphere of competence, has made a reasonable interpretation of section 4(a)(2) [of the Act]." *Id.* at 19a. Accordingly, the court of appeals' unexceptionable application of the *Chevron* framework warrants no further review.[11]

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tion, rather than the analysis, of the court's opinion. Early in its opinion, before recounting an analysis of the Act's terms, structure, and legislative history, the court did state that "[t]he question for us is whether the Board's interpretation of the language that does appear in the Act is reasonable." Pet. App. 12a. Petitioner thus asserts that the court erred in "mov[ing] hastily to step two [of the *Chevron* framework]." Pet. 13. But the court's opinion, when read in its entirety, shows that the court carefully considered the Act's language, structure, and legislative history before concluding that the statute was sufficiently ambiguous to warrant proceeding to determine whether the Board's construction was a permissible reading of the statute.

[11] Contrary to petitioners' submission, there does not appear to be any "wide-spread difficulty in the lower courts" concerning application of the *Chevron* framework. Pet. 14. In each of the decisions petitioners cite, the court proceeded to consider the reasonableness of the agency's construction of the statute only after determining, by traditional methodologies, that the pertinent statutory provision was sufficiently ambiguous. See *Lile* v. *University of Iowa Hosps. & Clinics*, 886 F.2d 157, 160 (8th Cir. 1989) (court determines that the term "governmental program" was "open to debate"); *National Ass'n of Casualty & Surety Agents* v. *Board of Governors*, 856 F.2d 282, 289 (D.C. Cir. 1988) (court concludes that "nothing in either the language or structure of the statute, or in the legislative history, conclusively resolves this dispute"), cert. denied, 109 S. Ct. 2430 (1989); *Securities Indus. Ass'n* v. *Board of Governors*, 807 F.2d 1052, 1056 (D.C. Cir. 1986) (court notes that agency "has comprehensively addressed the language, history, and purposes of the Act" and determines that "Congress has not clearly addressed the question [at issue]"), cert. denied, 483 U.S. 1005 (1987); *Verna* v. *Coler*, 710 F. Supp. 1339, 1341 n.2 (S.D. Fla. 1989) (upon review of language, legislative history, and purposes of Food Stamp Act, court was not "convinced that the term 'head of household' has a plain meaning"), aff'd per curiam, 893 F.2d 1238 (11th Cir. 1990).

2. Petitioners also renew their contention (Pet. 15-18) that Section 4(c)(8) of the Act, 12 U.S.C. 1843(c)(8), restricts bank subsidiaries of a bank holding company from selling insurance. By its terms, however, Section 4(a) of the Act, 12 U.S.C. 1843(a), speaks to a *bank holding company*'s ownership and control of *nonbanking* subsidiaries and *its* engagement in activities other than owning and managing banks. See p. 2, *supra*.[12] In other words, Section 4 does not restrict the kinds of *banks* that a bank holding company may own or control. For that reason alone, petitioners' construction of the statute is mistaken.

Moreover, Section 4(c) of the Act, 12 U.S.C. 1843(c), provides exemptions to the ownership and operational prohibitions otherwise contained in Section 4(a). The insurance restrictions in Section 4(c)(8), contrary to petitioners' submission, are not independent prohibitions on bank holding company activities. Those restrictions are only limitations on the exemption provided in Section 4(c)(8), namely, limitations on the Board's authority to expand bank holding company activity in areas "closely related to banking or managing or controlling banks." Section 4(c)(8) of the Act, 12

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[12] The operational restrictions set forth in Section 4(a)(2) of the Act, 12 U.S.C. 1843(a)(2), refer only to any "bank holding company"—not to any "bank." The Act defines the term "bank holding company" as a company that has control of any bank. 12 U.S.C. 1841(a)(1). This definition denotes the parent company itself, as opposed to the holding company system as a whole. Accordingly, petitioners err in reading Section 4(a)(2)'s operational restrictions as applying not only to activities conducted directly by the parent bank holding company, but also to activities conducted indirectly by any subsidiary of that bank holding company. Moreover, petitioners' construction would make the ownership restrictions in Section 4(a)(1) and (2) superfluous. If a bank holding company were deemed to be engaged in each activity conducted by its subsidiaries, the ownership restrictions would be unnecessary because the subsidiaries' activities would also be subject to the operational restrictions in Section 4(a)(2).

U.S.C. 1843(c)(8). In other words, the ownership and operational prohibitions in Section 4(a), and the exemptions to those prohibitions in Section 4(c), limit the types of subsidiaries that bank holding companies may control to banks and authorized nonbanks.[13] Since Section 4(c)(8) cannot bear the weight petitioners would place on that provision, the court of appeals correctly rejected their construction of the Act.

3. Finally, petitioners (Pet. 8-12) and their amicus (Br. 3-11) overstate the practical significance of the court of appeals' decision. The decision means only that banks owned by bank holding companies may continue to provide services authorized by the chartering authority—an activity that many banks have engaged in since long before the enactment of the Bank Holding Company Act.[14] The ability

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[13] Petitioners' reliance on the "acknowledged purpose of Section 4," Pet. 16, the separation of banking and nonbanking businesses, is misplaced. In *Board of Governors* v. *Dimension Fin. Corp.*, 474 U.S. 361, 374 (1986), the Court eschewed such an approach to statutory interpretation, recognizing that "[i]nvocation of the 'plain purpose' of legislation at the expense of the terms of the statute itself takes no account of the processes of compromise and, in the end, prevents the effectuation of congressional intent."

Contrary to petitioners' assertion (Pet. 17-18), the Board has consistently held that the prohibitions in Section 4(a) do not apply to activities conducted directly by banks owned by bank holding companies. And petitioners err in suggesting that the Board's decision in *Citicorp (South Dakota)*, 71 Fed. Res. Bull. 789 (1985), applied those prohibitions to certain bank holding company banks. There, the Board found that the entity involved, although chartered as a bank, would be operating almost exclusively in nonbanking activity, namely, the insurance business. The Board determined that in those circumstances the entity did not qualify as a "bank" for purposes of the Act. Here, by contrast, there is no dispute that Merchants' subsidiaries, Mid State Bank and Anderson Bank, function primarily as traditional banks.

[14] For example, state-chartered banks in Indiana have provided general insurance services since 1916. See Pet. App. 6a.

of banks to conduct such activities, even if they are not permissible for bank holding companies, has been an accepted part of the regulatory framework since the passage of the Act. Moreover, federal regulatory authorities have ample means to assure that federally insured banks do not engage in nonbanking activities that pose undue risks to the federal insurance fund.[15] See, *e.g.*, 12 U.S.C. 1816 (FDIC may deny deposit insurance if bank's powers are inconsistent with deposit insurance legislation); 12 U.S.C. 1818(a) (FDIC may terminate deposit insurance if bank engages in unsafe or unsound practices); 12 U.S.C. 1818(b) (federal bank regulatory agencies may issue orders to restrain unsafe or unsound practices).[16] In these circumstances, and in light of the absence of any conflict in the lower courts over the question presented, further review by this Court is unwarranted.

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[15] For example, the FDIC has recently announced that it is considering imposition of limitations on insurance and real estate activities authorized for Delaware-chartered banks under a new state law. See Wall St. J., June 13, 1990, at A2, cols. 3-4 (eastern ed.).

[16] The concern that the court of appeals' decision will invite abusive anticompetitive "tying" of various services offered by banks is particularly out of place. See Pet. 10-11; Amicus Br. 5-10. Congress has already explicitly prohibited such practices. See 12 U.S.C. 1971 *et seq.*

CONCLUSION

The petition for a writ of certiorari should be denied.
Respectfully submitted.

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Intervenor.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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PETITIONERS' REPLY BRIEF

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PETITIONERS' REPLY BRIEF *

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* Pursuant to Rule 28.1, the petitioners state that the National Association of Professional Insurance Agents, only, has a parent company, subsidiary (other than wholly-owned), or affiliate. That subsidiary is Certified Professional Insurance Agent, Inc.

1. That this petition presents questions of considerable national importance is demonstrated by the diverse amici briefs submitted to this Court. The insurance supervisory officials of the 50 states contend vigorously that the Second Circuit ruling undermines and obstructs their efforts to regulate the insurance industry in the public interest. *See Brief of the National Association of Insurance Commissioners as Amicus Curiae in Support of Petition for Writ of Certiorari* at 4. The state banking regulators of the 50 states contend, equally vigorously, that they are capable of overseeing the entry of a bank holding company's subsidiary bank into nonbanking businesses. *See Brief of the Conference of State Bank Supervisors as Amicus Curiae in Support of Respondent* at 2-3. The location of the federal-law boundary between these two classes of regulators is the exact question decided, wrongly, by the court below.

The ill-effects of the Second Circuit decision are not confined to insurance sales. The American Council of Life Insurance and the National Association of Realtors describe the adverse impact of bank holding company entry into the risky areas of insurance underwriting and real estate development. Indeed, bank involvement in real estate development, even when confined to traditional lending activities, already threatens the banking system. The value of leading bank stocks has fallen, "Sharp Retreat In Stock Prices Of Major Banks," American Banker, July 24, 1990, at 1; troubled real estate loans have cut bank earnings in the first quarter of 1990 by more than one billion dollars, "Problems with Real Estate Loans Held Back Earnings in 1st Quarter," American Banker, June 13, 1990, at 1, and continue to threaten the banking system with serious losses, *see* "Nonperformers, Foreclosures, Take Toll at Biggest Banks," American Banker, Aug. 7, 1990, at 8 ("The bottom fell out of the real estate portfolios of the nation's 10 largest banks in the first half of the year as the big banks racked up massive non-

performing loans . . . .") ; and bad real estate loans led to the federal takeover of the lead bank of a major—now bankrupt—Washington D.C. bank holding company, "Regulators Take Over D.C. Bank," Washington Post, Aug. 2, 1990, at 8.

The entry of bank holding companies into real estate development and other risky activities can only exacerbate the trouble. Even now, the Conference of State Bank Supervisors explains that five states allow insurance underwriting, twenty-four states permit real estate equity participation and development, and seventeen states authorize securities underwriting. Appendix 1, *Brief of the Conference of State Bank Supervisors as Amicus Curiae in Support of Respondent* at 2-3.

The practical importance of the question whether federally-regulated banking institutions can expand into a wide area of risky activities grows day-by-day. Since the petition for certiorari was filed, the Chairman of the Federal Deposit Insurance Corporation has admitted that the federal deposit insurance fund for commercial banks is under "considerable stress," and could lose as much as $2 billion by year's end. "Health of FDIC Being Exposed To the Spotlight," American Banker, July 25, 1990, at 1. Chairman Seidman's comments were made amid speculation that the FDIC is already insolvent. "Economist Says 'Insolvent' FDIC is Covering Up," American Banker, July 5, 1990, at 1.

Meanwhile, the S&L crisis deepens. The Government Accounting Office estimates that the clean-up could cost as much as $500 billion. "FSLIC Deficit Tops $87 Billion, RTC Costs Could Hit $500 Billion, GAO Says," Banking Report (BNA), p. 146 (July 23, 1990). And the evidence is clear that liberal state laws authorizing thrift entry into nonbanking areas, most notably real estate development, contributed directly to the current crisis. "For S&L Industry, Bailout Bill May Be A Fatal Blow," Los Angeles Times, Aug. 5, 1990, at A1.

Against this backdrop, the Solicitor General contends that an interpretation of the BHC Act permitting federally-regulated bank holding companies to enter non-banking businesses through liberal state banking laws raises no significant national issue. He relies on the fact that the Federal Deposit Insurance Corporation assertedly has authority that could be used to guard against the risks of bank expansion. But events have overtaken the Solicitor General's assurances. Since a new law to permit insurance activities was enacted in Delaware on May 30, 1990, Citicorp, the nation's largest bank holding company, has quickly taken steps to underwrite and sell insurance across the nation. "Citibank Comes to Kent County," Delaware State News, June 23, 1990, at 1. The FDIC is studying the problem, but has yet to take any action. "FDIC Appears Flexible on Insurance Issue," American Banker, June 18, 1990, at 1.

Had the petitioners' interpretation of the BHC Act been applied by the Second Circuit, today's situation would be drastically different. Because the BHC Act clearly and specifically bars general insurance activities, 12 U.S.C. § 1843(c)(8), application of the Act to bank holding companies in Delaware would have precluded the first stirrings of general insurance activity. There would have been no need, in other words, to hope that the FDIC would chase the horse after it escaped from the Federal Reserve Board's barn.

2. The Solicitor General acknowledges that the Second Circuit asserted the need to defer to the Board "before recounting an analysis of the Act's terms, structure, and legislative history," Brief for the Federal Respondent in Opposition at 12 n.10, but contends, nonetheless, that the Second Circuit applied the two-part *Chevron* standard in an unexceptional fashion. This Court's recent decisions demonstrate the error in that view. In *Maislin Industries v. Primary Steel, Inc.*, —— U.S. ——, 58 U.S.L.W. 4862, 4865 (U.S. June 19, 1990), the Court fully analyzed the

meaning of the relevant statute and, upon finding the meaning clear, refused to move past the first prong of the *Chevron* standard to grant the agency's plea for deferential review. In applying the first step, the Court was careful to note that the agency's interpretation "undermines the basic structure of the Act," and "conflicts directly with the core purposes of the Act." *Id.* at 4866. Similarly, in *Eli Lilly and Company v. Medtronic, Inc.*, —— U.S. ——, 58 U.S.L.W. 4838, 4840, 4842 (U.S. June 19, 1990), the Court looked closely at the structure of the relevant act and the plausibility of the proffered interpretation in order to determine the correct statutory meaning.

The failure of the Second Circuit to apply a similarly sophisticated approach was outcome determinative. That court found that (i) the Board's interpretation conflicts with the only identified statutory purpose, (App. A at 11a), (ii) the Board's major structural argument is "perplexing," (App. A at 14a), and (iii) the practical effect of the Board order is clothed with "apparent awkwardness and perhaps illogic," (App. A at 15a). Only because it deferred before it deliberated, by skipping the first step of the *Chevron* standard, was the court able to affirm the Board's interpretation.

3. The Solicitor General's attempt to defend the merits of the Board's interpretation largely rests on grounds rejected by the Second Circuit. The fact that Section 4(a) refers to "bank holding companies" and not to "banks," *Brief for the Federal Respondent in Opposition* at 13 & n.12, "somewhat begs the question, which is whether the limitation upon bank holding companies should be interpreted to restrict the activities those entities may engage in *indirectly* through their banking subsidiaries," App. A at 12a (emphasis in original). Moreover, notwithstanding the Solicitor General's assertion to the contrary, *Brief for the Federal Respondent in Opposition* at 13-14, the express insurance limitations of Section 4(c)(8) en-

tirely support "[t]he available inference . . . that subsidiary banks are subject to the 'activities clause' [of Section 4(a)] because they are within the category of entities exempted from that clause by section 4(c)(8)," App. A at 14a. The Solicitor General fails even to respond to the simple point that this Court has previously affirmed the Board's power to regulate the activities of subsidiary banks as part of its general power to regulate the nonbanking activities of a bank holding company. *See Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981); *Petition* at 9 n.4 & 18 n.10.[1]

CONCLUSION

For the reasons stated herein and in their Petition, the petitioners respectfully request that the petition for a writ of certiorari be granted.

Respectfully submitted,

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August 13, 1990

[1] Merchants National Corporation and the Conference of State Bank Supervisors continue to advance interpretations of the Bank Holding Company Act that have been uniformly ignored by the Board, the Second Circuit and now the Solicitor General. They are entitled to no further weight by this Court.

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BRIEF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS AS AMICUS CURIAE IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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INTEREST OF THE AMICUS CURIAE

The National Association of Insurance Commissioners ("NAIC") is a nonprofit, unincorporated association whose membership consists of the insurance supervisory officials of the 50 states, the District of Columbia, the territories and insular possessions of the United States. The NAIC was organized in 1871 to assure the protection of policyholders across the country. As stated in the NAIC's Constitution, the protection of policyholders continues to be the principal objective of the NAIC:

> "Article II. OBJECTIVE
>
> The objective of this body is to serve the public by assisting the several State insurance supervisory officials, individually and collectively, in achieving the following fundamental insurance regulatory objectives:
>
> (1) Maintenance and improvement of State regulation of insurance in a responsive and efficient manner;
>
> (2) Reliability of the insurance institution as to financial solidity and guaranty against loss;
>
> (3) Fair, just and equitable treatment of policyholders and claimants."

II NAIC *Proceedings*, p. iv (1989).

The principal function of the NAIC and each insurance commissioner is to serve the public by assisting these insurance commissioners in overseeing the activities of the insurance industry.

In submitting this brief, the NAIC seeks to demonstrate its interests in this proceeding, which are:

1. To preserve the orderly regulation of insurance in the respective states;

2. To assist the state insurance commissioners in protecting the interests of consumers across the country by preventing inherent coercion and tying arrangements.

At issue in this case is: do non-banking limitations of the Bank Holding Company Act, 12 U.S.C. §§ 1841-1850, apply when a bank holding company engages in non-banking activities through direct ownership and operation of a state-chartered subsidiary bank that sells insurance?

Since the Second Circuit decision has immediate and nationwide consequences, the question presented is a novel one. It has great public importance. The NAIC supports the legal arguments set forth in Sections I, II and III of the Reasons for Granting the Writ of the Petitioners' petition for a writ of certiorari. Additionally, the NAIC respectfully advances some additional arguments of its own. These arguments are set forth below.

This brief is therefore submitted, with written consent of the parties, in support of the petitioners.

ARGUMENT

I. THE SECOND CIRCUIT DECISION CREATES A SIGNIFICANT NATIONWIDE IMPACT ON ALL STATE INSURANCE COMMISSIONERS.

Congress has separated the banking industry and insurance industry for two basic reasons. Those reasons

are: to preserve the financial stability of both industries and to protect their respective customers.

A. THE STATE INSURANCE COMMISSIONERS SEEK TO MAINTAIN THE ORDERLY AND UNIFORM REGULATION OF INSURANCE.

In urging this Court to grant the Petitioners' petition, the NAIC seeks to maintain the orderly and uniform regulation of insurance. The regulation of insurance will be severely hampered if the Second Circuit decision stands. The decision will create numerous problems for insurance commissioners. The two primary problems include: inherent coercion and tying arrangements. In addition, regulatory lines of authority may be blurred.

The regulation of the business of insurance in the United States is left exclusively to the states, pursuant to the McCarran-Ferguson Act, 15 U.S.C. § 1012. On the other hand, banks and other types of financial institutions are regulated by a combination of state and federal banking regulators pursuant to 12 U.S.C. § 1846. Whatever may be the history of federal-state relations in other fields, regulation of banking has been one of "dual" control since the passage of the first National Bank Act of 1864 (13 Stat. 99). *See, National State Bank v. Long,* 630 F.2d 981, 985 (3d Cir. 1980).

The NAIC argues that despite the obvious intent of the law, the Federal Reserve Board of Governors' ("Board") authorization is in excess of its statutory authority. The Board does not have jurisdiction over the activities of a state-chartered bank selling insurance.

Section 4(c)(8) of the Bank Holding Company Act,[1] clearly prohibits all parts of a bank holding company from engaging in insurance activities.

B. THE SECOND CIRCUIT DECISION WILL ALLOW FOR "INHERENT COERCION."

If the Second Circuit decision is allowed to stand, banks and their subsidiaries will use their inherent ability to coerce customers into believing that the purchase of insurance will help them to secure and maintain credit. This would be especially true where the existence of a small business is heavily dependent on a continued source of credit. Coercion is inherent in such situations.

The NAIC argues that allowing banks to sell all types of insurance will result in the practice of coercing joint purchases. In general, the consumer is not so knowledgeable concerning these activities to avoid them. The same considerations relating to the tying of credit life insurance to the extension of credit applies to other types of insurance. Under the Second Circuit decision, banks will still be able to engage in this type of activity regardless of the amount of bank regulation prohibiting this type of activity.

C. THE SECOND CIRCUIT DECISION WILL ALLOW TYING AGREEMENTS.

In addition to this inherent coercion factor, the NAIC argues that tying will occur if the Second Circuit decision

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[1] 12 U.S.C. § 1843(c)(8).

is not overturned. Tying is defined as the sale of a principal product or service (the tying good) upon the condition that the consumer also purchase an ancillary product or service (the tied good) taken from a multi-product seller. Tying arrangements under this definition may take two forms.

First, it may be involuntary; that is, the seller may explicitly coerce the joint purchase. If this occurs, the bank or its subsidiary would be in violation of Section 106 of the Bank Holding Company Amendments of 1970[2] or Section 3 of the Clayton Act.[3]

Second, tie-ins may be voluntary as the joint purchase may occur based upon the consumer's perception that it would increase charges for obtaining the tying product from an implied or indirect suggestion for obtaining the tying product from an implied or indirect suggestion of the seller. This would occur without the buyer being aware that he had purchased the tied product. Voluntary tying (which is also illegal), if proven, is a practice that is elusive and difficult to demonstrate in a court of law.

The State of New York at one time considered implementing prohibitions on lenders who require the purchase of insurance in connection with a loan through a specified agent or from a particular insurer.[4] This proposed legislation included the following additional safeguards against tie-in sales:

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[2] 84 Stat., at 2065.

[3] 15 U.S.C. § 3.

[4] A.B. 5965, S.B. 3428 (Governor's Program Bill No. 31).

- Lenders who sell insurance would be prohibited from soliciting insurance from prospective borrowers prior to approval of their credit application;

- Lenders would be required to provide a 30-day cancellation privilege for policies sold in connection with extensions of credit;

- Lenders would be required to provide a disclosure form to prospective borrowers, together with the credit application, that spells out the customer's rights in connection with the purchase of any insurance required as part of a loan transaction;

- Lenders would be required to accept any policy meeting the lender's objective and uniformly applied minimum standards relating to the coverage required;

- Lenders would be prohibited from engaging in delaying tactics that would penalize borrowers who obtained insurance coverage through agents or brokers or insurers of their own choice not affiliated with the lender; and

- Lenders would be prohibited from charging unreasonable fees in connection with the substitution of an insurance policy.[5]

Under this proposal, the New York Superintendent of Insurance would have the authority to suspend or revoke a bank's insurance license if it engages in anti-competitive practices in the sale of insurance in connection with the making of loans. The Superintendent also would have the authority to obtain an injunction under the Insurance

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[5] "Banks and Insurance: Concerns of a State Regulator," 6 J. of Ins. Reg. 176, 182 (Dec. 1987).

Law against such a bank and could request the Attorney General to bring a civil action on behalf of the people of the State for recovery of treble damages.

The NAIC argues that if the Second Circuit decision is left standing, banks will be able to engage in both types of tying practices because the banking institutions will restrict the consumer's freedom of choice.

Regulation Z, 12 C.F.R. § 226.4(d) (1981), provides that charges for credit insurance must be included in the finance charge. The NAIC further argues that, even though this law makes tying illegal, the sale of other types of insurance by banks will make it extremely difficult to prove and prevent such activities.

When insurance commissioners consider the question of banks selling insurance, the only experience they have had with this type of activity is the sale of credit insurance by the banks. Their response is as follows:

> " . . . Where else can [the insurance commissioner] look to see how the banks will act with regard to the well being of their clients? [The insurance commissioner has] had a great deal of experience with this subject in the state of Tennessee, and in our opinion the banks have acted in an abysmal manner, showing total disregard for their customers. The state of Tennessee had one of the highest prima facie rates for credit life insurance in the United States. For five years [the insurance department] attempted to lower this rate in the General Assembly and were fought tooth and nail by the banks, automobile dealers and finance companies every step of the way. The banks hired a series of the most effective lobbyists in Tennessee to bottle up this legislation. The fact that they were making

> enormous profits on this business did not deter them from wanting to continue to overcharge their customers for as long as they could get away with it.
>
> This is equally true in almost all other states in the Union. [The Tennessee Insurance Commissioner knew] of no occasion where the banks in a statesmanlike manner suggested that a reasonable price be put on credit life insurance for the benefit of consumers. In 1983 the bank holding companies even proposed to the Federal Reserve System the elimination of the very small differential that bank holding companies are required to reduce the rate below bank operating companies. They argued that they were at a competitive disadvantage by being unable to charge the higher price to their customers. They felt they had as much right to charge the high credit insurance rates as anyone else."[6]

Under the Second Circuit decision nothing prohibits the bank from selling these other types of insurance products or engaging in the above described activities. The banks claim, with all of the bank regulations, that such activity will not occur. This is not the case. The issue really is, can the insurance commissioner detect these violations, and if so, how can he or she remedy the violations?

Banks want to convince the insurance commissioners under the Second Circuit decision that they will not mishandle traditional insurance products in the same manner that they mishandled credit life insurance. In fact, they even make the point that they will not be able to

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[6] "Tennessee Commissioner Comments on Sale of Insurance in Bank Lobbies; Use of Percentage Leasing Agreements," 4 J. of Ins. Reg. 91, 92 (Mar. 1986).

charge consumers, in the same manner as credit life insurance, because the market will not permit them to do so. If the bankers are incorrect, the insurance commissioners will find it difficult to protect the consumers.

II. THE SECOND CIRCUIT DECISION WILL AFFECT A NUMBER OF PENDING BILLS IN STATE LEGISLATURES.

The issue presented in the Petitioners' petition is one of widespread significance. This case merits review by this Court because of a number of pending bills spawned from the Second Circuit decision. There are over 11 states currently in the process of considering enacting legislation that will allow state chartered banks to sell and underwrite insurance. In the state of Delaware, H. B. 193 was enacted into law on May 30, 1990.[7] This legislation allows banks to underwrite and sell all forms of insurance. More specifically, it authorizes Delaware banks to sell and underwrite all types of insurance directly within the bank rather than through the use of a legally separate subsidiary. In the past, banks would use a legally separate subsidiary to conduct their non-banking activities, especially those activities that entail a significant degree of risk. In addition, state and federal regulators have generally concluded that it is virtually impossible to effectively insulate a bank from its non-banking businesses where those activities are conducted within the same legal entity.

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[7] P.L. 90-223.

Out-of-state banks were instrumental in drafting Delaware H. B. 193. Those banks were very conscious of the corporate structure set out in the legislation. The language allows these entities to side-step federal banking law prohibitions on insurance activities. These prohibitions and the Second Circuit decision are in fact directed at the very activities Delaware H. B. 193 authorizes. The legislation also allows out-of-state banks to circumvent federal banking laws.

The Second Circuit decision thus provides the framework for similar pending legislation which is a scheme that places form over substance in an effort to evade federal banking law limitations on insurance. It creates a banking subsidiary that is really an insurance subsidiary which can engage in inherently coercive acts and tying arrangements.

SUMMARY OF ARGUMENTS

The NAIC vigorously supports the Petitioners' petition to this Court, requesting resolution of this issue. The impact of the Second Circuit decision is nationwide. In light of the pending legislation in several states and the impact that the Second Circuit decision will have on "insurance regulation," the NAIC respectfully requests a review of that decision by this Court.

CONCLUSION

For the foregoing reasons, the NAIC respectfully requests that this Court grant the Petitioners' petition for certiorari.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., AND THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

Petitioners,

v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM AND MERCHANTS NATIONAL CORPORATION,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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BRIEF OF THE AMERICAN COUNCIL OF LIFE INSURANCE AS AMICUS CURIAE IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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IN THE

Supreme Court of the United States

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No. 89-1620

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., AND THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

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BRIEF OF THE AMERICAN COUNCIL OF LIFE INSURANCE AS AMICUS CURIAE IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

INTEREST OF THE AMICUS CURIAE

The American Council of Life Insurance ("ACLI") is a trade association of 616 stock and mutual life insurance companies. Collectively, ACLI represents a total of approximately 94 percent of the nation's life insurance

companies. ACLI has long been active in administrative, legislative, and litigation matters regarding the permissible scope of bank insurance activities. *Amicus* has a strong interest in this case because its members likely will suffer substantial competitive injury if the order of the Federal Reserve Board ("Board"), as affirmed by the court of appeals, is not reviewed. *Independent Insurance Agents of America, Inc. v. Board of Governors*, 890 F.2d 1275 (2d Cir. 1989).[1]

By permitting bank subsidiaries of bank holding companies to sell insurance products, the Board misinterpreted Congress' clear direction that bank holding companies and their subsidiaries shall not generally engage in insurance related activities. The Board's order erodes the barriers between banking and insurance which Congress erected to ensure stability and fairness in financial markets, and in the insurance industry. Because the Board's order creates a major loophole in the Bank Holding Company Act ("the BHC Act" or "the Act"), its significance extends far beyond the ability of banks to sell insurance.

If this Court does not review the Board's order, it risks the degradation of the nation's banking system into a chaotic patchwork of competing state regulations. By acquiring a subsidiary bank in the correct state, bank holding company systems will be free to plunge into nationwide insurance underwriting activities that Congress has judged too risky for banks in holding company form. Indeed, under heavy pressure from banking interests, states already have begun a "race for the bottom," with the "winners" expanding greatly the powers of state-chartered banks. The resulting expansion of bank holding company activities is precisely what Congress in-

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[1] Pursuant to Rule 37 of the Rules of the Court, the parties have consented to the filing of this brief. Their letters of consent have been filed with the Clerk of the Court.

tended to prohibit through the Bank Holding Company Act.

SUMMARY OF THE ARGUMENT

The Bank Holding Company Act of 1956 regulated bank holding companies that previously had been free to engage in nonbanking as well as banking activities. Congress observed that the assimilation of independent banks into large holding company conglomerates allowed bank holding companies to magnify their economic power and embark on nationwide commercial ventures. Recognizing that such activity could pose a substantial danger to the soundness of the banking system and to the competitive position of commercial enterprises that were not part of a financial institution conglomerate, Congress adopted the BHC Act to restrict bank holding companies to banking and "closely related" activities. In so doing, Congress carefully balanced competing policy concerns: it permitted independent banks to choose whether to enjoy the benefits of bank holding company affiliation, but prohibited those that did so from engaging in commercial, nonbanking activities.

The Board's order destroys this legislative balance. The Board now disclaims any authority to prevent a bank subsidiary of a bank holding company from engaging in nonbanking activities. Yet the Board continues to claim the power to prevent commercial activities by (i) nonbank subsidiaries of a bank holding company, (ii) nonbank subsidiaries of a bank subsidiary of a bank holding company, and (iii) a bank holding company.

This "perplexing" result suffers from several critical flaws. *First*, the decision below essentially disregards the entire purpose of the BHC Act, and creates a mechanism for avoiding that statute by transferring otherwise forbidden activities to a state bank in any state permitting the activity. Indeed, the decision below perversely maximizes the resulting risks to banks, to depositors, and to federal deposit insurance.

Second, by inciting states to curry favor with powerful banking interests in order to attract or maintain banking industry jobs and tax revenues, the Board's order is a powerful spur in a regulatory "race to the bottom" that undermines uniform national regulation of bank holding companies. The resulting legal patchwork will be the opposite of the uniform national regulation which Congress intended.

Finally, in affirming the Board's order, the court of appeals recognized some of its irrationality, but erroneously deferred to the Board's construction of the statute. That judicial abdication was based on an unfortunate misunderstanding of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). As this Court reaffirmed in *INS v. Cardoza-Fonseca*, 480 U.S. 421, 449 (1987), deference to agency policy does not arise under *Chevron* until the court has employed the "traditional tools of statutory construction" —including "analysis of the plain language of the Act, its symmetry [with other legislation], and its legislative history." Those traditional tools of statutory construction establish the Board's error in this case. Moreover, no deference should be given to inconsistent agency interpretations—and the Board's order is contradicted by the Board's own regulations.

Because this case involves issues that are vitally important to the nation's bank regulatory system, and because its practical ramifications for banking and nonbanking industries alike are profound, this Court should grant certiorari.

ARGUMENT

I. CONGRESS ENACTED SECTION 4 OF THE BANK HOLDING COMPANY ACT TO LIMIT BANK HOLDING COMPANY COMPLEXES TO BANKING AND ACTIVITIES "CLOSELY RELATED" TO BANKING

In section 4 of the Bank Holding Company Act, Congress forbade bank holding companies and their subsidiaries generally from "engag[ing] in any activities other than (A) those of banking . . . and (B) those . . . [activities which are] so closely related to banking . . . as to be a proper incident thereto." 12 U.S.C. § 1843. Under section 4, bank holding companies may "acquire" or "retain", either directly or indirectly, only "banks" and other companies engaged in activities "so closely related to banking . . . as to be a proper incident thereto." *Id.*

The principal question here is whether the Act's prohibition on non-banking activity by bank holding companies applies to the actual banks owned by the bank holding companies. The court of appeals concluded that no statutory phrase definitively resolves this question. 890 F.2d at 1281. Although the Act's terms provide square support for petitioners' construction, Pet. at 15-17, the Board's order is glaringly inconsistent with the goals, legislative history and policy of the Bank Holding Company Act. No clever parsing of words and phrases can justify a decision that is so totally at war with the underlying thrust of the statute being interpreted.

A. The Goals And Legislative History Of The Bank Holding Company Act Are Directly Contrary To The Decision Below

Beginning in the 1950s, Congress became concerned that the nation's banking system was being misused and undermined by unregulated holding companies which combined both banks and completely unregulated non-bank companies. Congress concluded that this combina-

tion of bank and nonbank companies posed distinct dangers for the national economy, including: (i) the risks to banks whose fate became intertwined with the nonbanking commercial activities of the holding company; (ii) the linking of bank credit to patronage of the holding company's nonbanking enterprises; and (iii) the increased economic power of banks that became part of holding company conglomerates. *See* S. Rep. No. 1095, 84th Cong., 1st Sess. 5, 10, 14, *reprinted in* 1955 U.S. Code Cong. & Admin. News 2482, 2486, 2491-92, 2495; *see* H.R. Rep. No. 609, 84th Cong., 1st Sess. 16-17 (1955). In order to minimize these dangers, Congress approved the 1956 Act.

The Act aimed to halt the misuse of and damage to the banking system by codifying for bank holding companies the core principle that "banking institutions should not engage in business wholly unrelated to banking." S. Rep. No. 1095, 84th Cong., 1st Sess. 2 (1955); *see also* H.R. Rep. No. 609, 84th Cong., 1st Sess. 16 (1955). As this Court has observed, one of the "primary objectives" of the 1956 Act was "to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity." *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980).

The Act's legislative history amply reflects the congressional purpose to require the divestiture not only of nonbanking "companies" but also of nonbanking "enterprises," "interests," "businesses," and "activities" generally. *See, e.g.*, S. Rep. No. 1095, 84th Cong., 1st Sess. 1, 4, 5, 13-14, 21. Conversely, the legislative history is devoid of any indication that Congress intended to permit *any* component of a bank holding company complex, including bank subsidiaries, to engage in any activity other than banking or activities closely related to banking.

Later Congresses have confirmed the view that the 1956 Act prohibits nonbanking activities conducted di-

rectly by the holding company *or* through a subsidiary. For example, in 1970 Congress extended the Act to bank holding companies with only one constituent bank. At the same time, Congress enacted a "grandfather" exception providing that a bank holding company may continue to "engage in those activities in which *directly or through a subsidiary . . . it was lawfully engaged* on June 30, 1968." 12 U.S.C. § 1843(a)(2) (emphasis supplied). The 1970 statute also gave the Board the power, under certain circumstances, to "terminate the authority conferred" by this proviso. Congress thus understood that the 1970 grandfather provisions "conferred" on a few institutions the authority to carry on commercial activities through subsidiaries, and that the general prohibition of Section 4(a)(2) otherwise barred the conduct of such activities through subsidiaries.

In 1982 amendments, Congress directed that general insurance activities, with limited exceptions, are too far removed from banking to be conducted by bank holding companies. Garn-St Germain Depositary Institutions Act of 1982, Pub. L. No. 97-320, § 607, 96 Stat. 1469, 1536-38 (1982). Congress thus repeated one more time its insistence that banking institutions and their depositors must be protected from the adverse financial consequences that could arise from business activities wholly unrelated to banking. The Conference Report confirms that the 1982 amendments "generally prohibit[] bank holding companies *and their subsidiaries* from providing insurance." H.R. Conf. Rep. No. 899, 97th Cong., 2d Sess. 9 (1982) (emphasis supplied). The conclusiveness of this passage is underscored by the Act's definition of "subsidiary," which explicitly encompasses "banks." 12 U.S.C. § 1841(b-d). Surely, if the Conference Committee had intended to refer only to nonbank subsidiaries, it would have done so.

B. *Merchants National* Perversely Maximizes The Risk Of Non-banking Activities

The Board's order yields the completely perverse outcome that non-banking activities may be conducted directly in the bank, where the risk to depositors and federal deposit insurance funds is *greatest*. Were a bank to engage in commercial ventures through a subsidiary, the limitation upon liability provided by the corporate form would insulate the bank's assets from the bank's nonbanking losses. But the Board's order ensures that no such protection will be available, thus maximizing the risk of loss to depositors and taxpayers. *See also* Blueprint for Reform: The Report of the [Bush] Task Group on Regulation of Financial Services (1984), Fed. Sec. L. Rep. (CCH) No. 1099, Pt. 2 at 47 (noting the "importance of conducting nonbanking activities in separate holding company subsidiaries rather than in the bank itself"); 50 Fed. Reg. 23,964 (June 7, 1985) (FDIC advocated prohibiting insured banks from directly engaging in insurance). This result is precisely the opposite of Congress' intent to protect banks, depositors, and federal deposit insurance from the risk of commercial nonbanking activities.

The perversity of this outcome was recently underscored by—of all people—the Chairman of the Federal Reserve System, who expressed concern that "permitting banking organizations to engage in a larger number of activities will spread the [federal deposit insurance] safety net ever wider and wider through a network of bank affiliates." Remarks before the Annual Conference on Bank Structure and Competition, May 10, 1990, pp. 10-11. The Chairman warned banks *not* to conduct high-risk activities directly in the bank, but to build "firewalls" protecting the bank's assets by placing high-risk activities in separate subsidiaries (*id.* at 11):

> [s]uch an extension [of the deposit insurance safety net] would threaten to intensify the adverse effects

of suppressing market signals, and raise questions about what the safety net is designed to protect. By design, firewalls should avoid the extension of the safety net, keeping it under the commercial banks alone.

The Board's order flies in the face of the Chairman's wise counsel, compelling bank holding companies to conduct risky nonbanking activities directly within their subsidiary banks, with no "firewalls" at all. This case illustrates this perverse process. It began with an application by Merchants National Corporation ("Merchants") to acquire Mid-State Bank of Danville, Indiana ("Mid-State"), which had conducted insurance agency business through a wholly-owned subsidiary. Merchants initially proposed that Mid-State conduct the insurance agency activities through its subsidiary, leaving intact the "firewall" between the bank and the insurance activity of its subsidiary. But Merchants then amended its proposal to bring the insurance activities directly into the bank, with no firewall at all, in order to avoid the nonbanking prohibitions of the BHC Act. 75 Fed. Res. Bull. 388, 390 n.9 (1989). Nothing in the statutory text or legislative history supports this perverse outcome.

II. THE DECISION BELOW UNDERMINES NATIONAL REGULATION OF BANK HOLDING COMPANIES AND WILL TRIGGER A REGULATORY "RACE TO THE BOTTOM" AMONG THE STATES

Taking advantage of the loophole created by the Board's order, bank holding companies and their constituent state banks are spurring a headlong "race to the bottom" of bank regulation. Less than three weeks after the Board's decision, the minority leader of the Delaware General Assembly introduced legislation permitting Delaware-chartered banks to engage directly in every aspect of insurance underwriting and agency, and to do so on a nationwide basis. *See* "Banks Strike at Insurance Legislation While Iron is Hot," *The* [*Delaware*] *News Jour-*

nal, April 9, 1989, p. D3. With similar legislation already pending in California and Florida, Delaware legislators sought to act quickly to attract big bank holding companies to Delaware. *Id.*

In mid-May, while "more than a dozen bank lobbyists clogged the corridors of Delaware's Legislative Hall in Dover," the Delaware legislators adopted broad legislation authorizing state banks to underwrite insurance. "Delaware Bill Opens Insurance to Banks," *Wall Street Journal*, May 21, 1990, p. A4. This legislation was signed into law by Delaware Governor Michael Castle on May 29, 1990. 54 *BNA's Banking Report* 946 (June 4, 1990).

The *Wall Street Journal* reported (May 21, 1990, p. A4) that the Delaware legislation "opens the door to huge money-center and superregional banks," and that "state officials have backed the measure because it holds the prospect of generating thousands of new jobs." The Chase Manhattan Corporation has already announced plans to convert its $8 billion Delaware bank from a federal charter to a state charter in order to take advantage of the new Delaware legislation. *See* "Delaware to Allow Banks to Sell Insurance," *The New York Times*, May 31, 1990, p. D17. Citicorp, the nation's largest banking company, has also announced plans to begin underwriting insurance in Delaware—a business which Delaware officials have estimated may employ more than 300 people. *Id.*

The race to the bottom is not confined to Delaware. Twelve states reportedly are considering legislation to let banks engage in insurance. 54 *BNA's Banking Report* 724 (April 30, 1990).

In recent congressional testimony, the Conference of State Bank Supervisors reported that the race to the bottom is in full swing. Delaware and North Carolina permit banks to underwrite both securities *and* insurance, while three other states permit insurance under-

writing and fifteen other states allow securities underwriting.

Twenty-two states allow banks to engage in *both* real estate equity participation and real estate development—both of which also carry high risks. Three states allow banks to engage in insurance, securities *and* real estate brokerage, while four states permit banks to engage in two of those brokerage activities, and twenty-one more states grant banks the power to engage in at least one such brokerage activity. Gilleran, Statement Before House Subcomm. On Financial Institutions Supervision, Regulation And Insurance, Attachment 2 (April 4, 1990).

Effective federal oversight over the proper boundaries of bank holding companies will be effectively eliminated if holding company conglomerates may engage, through their component banks, in whatever activities the fifty states severally allow. Despite the undeniable risks associated with underwriting and real estate development, pressure from powerful banks will hasten the race to the bottom. Indeed, if the Board's order is allowed to stand, "banking" will no longer have any meaning under the Bank Holding Company Act, but will come to mean whatever any of the several states determines.

The savings and loan crisis vividly illustrates Congress' wisdom in prohibiting banks from straying into such risk-laden activities. Massive losses rendered the Federal Savings and Loan Insurance Corporation effectively insolvent and have prompted the President to call for a comprehensive overhaul of the federal deposit insurance system. *See* "Bush Savings Plan Calls for Sharing the Cost Broadly," *The New York Times*, Feb. 7, 1989, pp. A1, D8. These unprecedented losses, which ultimately will be absorbed by the taxpayers, have been caused in part by lax state laws that allowed thrifts to engage in high-risk activities not traditionally performed by savings institutions. *See, e.g.*, Federal Deposit Insurance Corporation,

Deposit Insurance for the Nineties: Meeting the Challenge, at 314 (draft edition, January 4, 1989). The Bank Holding Company Act announces a national policy of eliminating such risks for bank holding companies, but that policy is entirely frustrated by the decision below.

III. THE SECOND CIRCUIT MISAPPLIED *CHEVRON U.S.A., INC. v. NATURAL RESOURCES DEFENSE COUNCIL, INC.*

The first question for a court to consider when reviewing an agency's construction of a statute is "whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter . . . ." *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842 (1984). The need for independent examination of legislative intent by the reviewing court is clear and has constitutional underpinnings: "[t]he *judiciary* is the final authority on issues of statutory construction . . ." *Chevron*, 467 U.S. at 843, n.9 (emphasis supplied). *See also FEC v. Democratic Senatorial Campaign Comm.*, 454 U.S. 27, 32 (1981); *Diamond v. Chakrabarty*, 447 U.S. 303, 315 (1980) ("once Congress has spoken it is 'the province and duty of the judicial department to say what the law is'"); *NLRB v. Brown*, 380 U.S. 278, 291-92 (1965); *Marbury v. Madison*, 1 Cranch 137, 177 (1803).

In determining whether the intent of Congress is clear, the reviewing court should employ "traditional tools of statutory construction," including examination of the applicable legislative history. *NLRB v. Food and Commercial Workers Union*, 484 U.S. 112, 124 n.20 (1987); *Cardoza-Fonseca*, 480 U.S. at 446 n.30. The second *Chevron* question—whether the agency's interpretation of the statute is reasonable—*never arises* if Congress' intent is clear.

The examination of Congress' intent must be more than merely perfunctory. This is particularly true where, as

here, the question involved is one of pure statutory construction and does not involve an agency's "formulation of policy [or] the making of rules to fill any gap left, implicitly or explicitly, by Congress." *Cardoza-Fonseca*, 480 U.S. at 445-446 (quoting *Chevron*); *see also Food and Commercial Workers Union*, 484 U.S. at 123; *NLRB v. Brown*, 380 U.S. at 292.

The court of appeals did not apply these principles properly. Immediately after noting, in essence, that no magic words in the statute specifically apply the Act's nonbanking restrictions to *bank* subsidiaries of bank holding company complexes, the court opined that "[t]he question for us is whether the Board's interpretation of the language that does appear in the Act is reasonable . . . ." 890 F.2d at 1281. Thus, the court considered the legislative history of the Act *only* in the context of whether the Board's interpretation was reasonable. The court of appeals never did construe the statute in the light of Congress' plain intent.

Moreover, the court's deference to the Board was entirely misplaced, since the Board's order cannot be reconciled with the Boards' own regulations. To earn judicial deference, an agency's statutory construction must at least be consistent. *See Watt v. Alaska*, 451 U.S. 259, 273 (1981); *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 858 n.25 (1975). But the Board has issued regulations under the Bank Holding Company Act which limit "a bank holding company *or a subsidiary*" to banking related activity. 12 C.F.R. § 225.21(a) (emphasis supplied). The regulations state that "subsidiary" has "the same meaning" in the regulations as in the BHC Act, which the regulations define as "a *bank* or other company that is controlled by another company, and refers to a direct or indirect subsidiary of a bank holding company." 12 C.F.R. § 225.2(m) (emphasis supplied). Thus, the Board's own regulations explicitly bar bank subsidiaries from nonbanking activity. The Board's order lamely attempts to wish away this fundamental in-

consistency by stating in a footnote that the regulation's "definition does not apply where the context otherwise requires." 75 Fed. Res. Bull. at 392, n.21. The Board never explains, however, what "context" suspends the regulatory definition for this case.

The Board has been more candid in admitting that its order is inconsistent with another regulation which allows a holding company bank to use a subsidiary to engage in any activity in which the bank itself legally may engage. This regulation, 12 C.F.R. § 225.22(d)(2)(ii), completely contradicts the Board's contention that subsidiaries of a bank may not engage in commercial activities; since the regulation states that subsidiaries can do whatever their parent banks can do, no such prohibition exists. Over a year ago, the Board admitted this inconsistency and proposed to revise the regulation to make it consistent with *Merchants National.* 53 Fed. Reg. 48,915 (December 5, 1988). Such regulatory incoherence, however, surely is entitled to no deference from the courts.

CONCLUSION

For all of the foregoing reasons, *amicus* urges that the petition for a writ of certiorari be granted and that the judgment of the Court of Appeals be reversed.

Respectfully submitted,

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June 25, 1990

No. 89-1620

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC., AND THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

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Intervenor.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF THE CONFERENCE OF STATE BANK SUPERVISORS AS AMICUS CURIAE IN SUPPORT OF RESPONDENT

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QUESTION PRESENTED

Whether the Second Circuit correctly decided that the Federal Reserve Board permissibly interpreted section 4 of the Bank Holding Company Act of 1956, as amended, when it concluded that that section does *not* preempt state law governing bank operations and therefore does not subject state-chartered banks that are controlled by bank holding companies to the Act's restrictions on insurance activities.

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,

Respondent,

MERCHANTS NATIONAL CORPORATION,

Intervenor.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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BRIEF OF THE CONFERENCE OF STATE BANK SUPERVISORS AS AMICUS CURIAE IN SUPPORT OF RESPONDENT

INTEREST OF AMICUS CURIAE

The Conference of State Bank Supervisors ("CSBS") submits this brief as *amicus curiae* in support of Respondent, the Board of Governors of the Federal Reserve Sys-

tem (the "Board"), and in opposition to the petition for a writ of certiorari to the United States Court of Appeals for the Second Circuit. CSBS is the professional association of state government officials responsible for chartering and regulating more than 10,000 state-chartered banking institutions in the 50 states and in Guam, Puerto Rico and the Virgin Islands.

CSBS has a vital interest in this case because Petitioners' argument raises a serious threat of preemption of state banking laws.[1] Currently, the laws of fourteen states authorize state-chartered banks to engage, either directly or indirectly through subsidiaries, in insurance activities not permitted to bank holding companies by section 4(c)(8), 12 U.S.C. § 1843(c)(8), of the Bank Holding Company Act of 1956, as amended, 12 U.S.C. § 1841, *et seq.* ("BHC Act").[2] Petitioners assert that the Board must apply the restrictions on insurance activities of section 4(c)(8) to all holding company-owned state-chartered banks *regardless* of state law.

REASONS FOR DENYING THE WRIT

I. INTRODUCTION

Petitioners make no effort to show that this case is worthy of review by the Supreme Court by demonstrating either that this case involves a conflict among the decisions of the United States courts of appeals or that the case is of national importance. Moreover, Petitioners' arguments that the Second Circuit incorrectly decided the case are without merit.

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[1] CSBS frequently appears before the courts to resist unauthorized efforts to preempt state banking laws and to help preserve the deference to state law which Congress has consistently mandated in banking.

[2] *See* The Conference of State Bank Supervisors, *State of the State Banking System* 10 (1989) (reproduced at Appendix I).

This case involves the reaffirmation by the Second Circuit of the long-standing supervisory role of the primary bank regulators—the Comptroller of the Currency (for national banks) or the states (for state-chartered banks) —over bank subsidiaries of bank holding companies. The Board's responsibilities under the BHC Act are properly confined to the complementary role of regulating the activities of bank holding companies and their *nonbanking* subsidiaries.

Petitioners' alarmist argument that the Second Circuit's opinion changes an established interpretation of the law and threatens to create a savings and loan industry-type crisis is unfounded. To the contrary, it has long been the practice of state bank chartering authorities to authorize state-chartered banks to engage in nonbanking activities. Such activities are freely authorized because they are not restricted by the BHC Act.[3] Consequently, it is the Petitioners who would create chaos in the banking industry by suddenly rendering widespread, existing practices of state-chartered banks illegal.

There is, moreover, no justification for Petitioners' argument that the problems in the savings and loan industry are a harbinger of what expanded powers would mean for state-chartered banks. History demonstrates that, notwithstanding their expanded powers relative to national banks, the rate of failure for state-chartered banks is lower than that for national banks.[4]

Petitioners also contend that the Second Circuit misapplied the test for judicial review of agency interpretation of their generic statutes as articulated by the Supreme Court in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). They argue

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[3] *See id.*

[4] *See id.* at 8 (reproduced at Appendix II).

that without reviewing the statutory language and congressional intent, the court "hastily" moved to the second step of the *Chevron* analysis and pronounced the Board's interpretation to be "permissible." Petitioners would impose upon reviewing courts a structural rigidity of opinion writing that *Chevron* does not require; a reviewing court is not required to disembody its analysis of Congressional intent from the agency's analysis of that intent.

It is also clear from the court's opinion that it did not regard the evidence of Congressional intent as being favorable to Petitioners. After a lengthy review of the language of section 4, the language and structure of other related provisions of the BHC Act, the legislative history of the Act, subsequent legislation, and related case law, the Second Circuit concluded that the Board's position was correct. Under these circumstances, the mode of analysis employed by the Court of Appeals does not raise "principles the settlement of which is of importance to the public as distinguished from that of the parties," and so is not worthy of Supreme Court review.[5]

II. THE SECOND CIRCUIT WAS CORRECT IN DEFERRING TO THE BOARD'S INTERPRETATION OF THE BHC ACT

In its review, the Second Circuit properly deferred to the Board's interpretation of the BHC Act. The Board had merely reaffirmed its long-standing interpretation of the BHC Act. Where, as here, that interpretation is within the agency's particular expertise, it is entitled to great deference.[6]

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[5] *Rice v. Sioux City Cemetery*, 349 U.S. 70, 79 (1955) (quoting *Layne & Bowler Corp. v. Western Well Works, Inc.*, 261 U.S. 387 (1923)). *See also Magum Import Co. v. Coty*, 262 U.S. 159, 163 (1923).

[6] *See Board of Governors v. Investment Co. Inst.*, 450 U.S. 46, 56 (1981).

In *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), this Court articulated a two-step analysis for judicial review of an agency's construction of the statute which it administers: first, to determine "whether Congress has directly spoken to the precise question at issue"; and second, if Congress has not directly addressed the question at issue, to determine whether the agency's answer is based on a "permissible construction of the statute." [7]

In applying the first step of the *Chevron* analysis, the Second Circuit concluded that the provisions of the BHC Act did not "reveal an unambiguous congressional intent concerning the precise question at issue." [8] Then, in conjunction with an analysis of other indicia of Congressional intent, the court simultaneously proceeded with the second step of the *Chevron* analysis and concluded, after examining the statutory language using traditional principles of statutory construction and examining the legislative policy and history, that the Board's interpretation was reasonable.

That is exactly what this Court did in *United States v. Riverside Bayview Homes, Inc.*, 474 U.S. 121 (1985), where a unanimous Court began its statutory analysis by referring to the deference to be given to the agency's interpretation:

> An agency's construction of a statute it is charged with enforcing is entitled to deference if it is reasonable and not in conflict with the expressed intent of Congress. *Chemical Manufacturers Assn. v. Natural Resources Defense Council, Inc.*, 470 U.S. 116, 125 (1985); *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-845 (1984). Accordingly, our review is limited to the question whether it is reasonable, in light of the language,

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[7] 467 U.S. at 842-43. Of course, if the Congressional intent is clear, the reviewing court must give effect to that intent. *Id.*

[8] Pet. App. 11a.

> policies, and legislative history of the [statute] for the Corps [of Engineers] to exercise jurisdiction over [certain] wetlands.[9]

The Second Circuit thus applied the *Chevron* analysis in precisely the manner applied by a unanimous opinion of this Court, first noting that the language of the statute, by itself, was insufficient to answer the question at issue, and then analyzing the legislative history and underlying policy of the statute in the course of reviewing the reasonableness of the agency's interpretation of the statute.[10]

Further, the preemption of state law urged by Petitioners is an extreme remedy and may not be undertaken unless clearly intended by Congress: "It will not be presumed that a federal statute was intended to supersede the exercise of the power of the state unless there is a clear manifestation of intention to do so."[11] The presumption against preemption of state law, absent a clear statement of Congressional intent, is especially strong when, as in this case, there has been a long-standing history of state regulation.[12]

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[9] 474 U.S. at 131.

[10] *Id.* at 131-35.

[11] *Schwartz v. Texas*, 344 U.S. 199, 202-203 (1952). *See Chicago & North Western Transportation Co. v. Kalo Brick & Tile Co.*, 450 U.S. 311, 317 (1981) ("Pre-emption of state law by federal statute or regulaiton is not favored" quoting *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142 (1963)).

[12] *CTS Corp. v. Dynamics Corp. of America*, 481 U.S. 69, 86 (1987) (where there is a long-standing prevalence of state regulation, Congress "would have said so explicitly" if it intended to preempt state law); *Hillsborough County v. Automated Medical Laboratories, Inc.*, 471 U.S. 707, 715 (1985) (where the federal government enters a field where there is a long-standing history of state regulation, there is a presumption that the "powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress" quoting *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977)).

III. THE SECOND CIRCUIT'S DECISION CORRECTLY ALLOWS THE NATIONAL AND STATE BANK REGULATORS TO REGULATE THE NONBANKING ACTIVITIES OF BANKS OWNED BY BANK HOLDING COMPANIES

For over a century, the central feature of bank regulation in the United States has been a dual banking system composed of national banks chartered by the Comptroller and state banks chartered by the states.[13] The several federal banking statutes create a comprehensive regulatory scheme in which state and federal banking agencies have well-defined and complementary roles. National and state-chartered banks, as permitted by their primary regulators, engage in various banking-related activities.[14] The question of whether those activities also are permissible for bank holding companies or their nonbank subsidiaries is unrelated and cannot affect the operating authority of state-chartered banks.

In enacting the BHC Act, Congress expressly confined the Board's regulatory authority to bank holding companies and, with respect to their subsidiaries, to only their previously unregulated *nonbanking* subsidiaries.[15] Section 4 of the BHC Act unequivocally excludes a bank

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[13] S. Rep. No. 1095, 84th Cong., 2d Sess., pt. 2, at 5 (1956). *See also Northeast Bancorp, Inc. v. Board of Governors*, 472 U.S. 159, 172-73, 177-78 (1985) (BHC Act was intended "to retain local, community-based control over banking").

[14] *See, e.g.*, 12 C.F.R. §§ 5.34, 7.7430 & 7.7490 (regarding activities permitted of national banks by the Comptroller); The Conference of State Bank Supervisors, *A Profile of State Chartered Banking* 180-182 (12th ed. 1988) (lists of activities permitted of state-chartered banks by the states).

[15] *See Cameron Fin. Corp. v. Board of Governors*, 497 F.2d 841, 845 (4th Cir. 1974); H.R. Rep. No. 609, 94th Cong., 1st Sess., 1-6 (1955); *Control and Regulation of Banking Holding Companies: Hearings on H.R. 2674 Before the Committee on Banking and Currency of the House of Representatives*, 84th Cong., 1st Sess. 13-14 (1955) [hereinafter cited as "*1955 House Hearings*"].

holding company's *banking* subsidiaries from regulation by the Board.[16] Moreover, this Court clearly has stated that section 4 does not empower the Board to regulate banks.[17]

The plain language of the BHC Act supports the Second Circuit's conclusion that section 4 does not apply to holding company-owned state banks. Section 4(a) prohibits (with certain specific exceptions) a bank holding company from acquiring or retaining ownership or control of any company "which is not a bank."[18] It is only companies that are *not* "banks" under the BHC Act that must limit their activities to those permitted by section 4(c)(8) in order to be acquired or retained by a bank holding company.

Petitioners argue that the prohibitions of section 4(c)(8) apply to *both* banking and nonbanking subsidiaries of a bank holding company. However, the language of section 4(c)(8) does not support this assertion. The introduction to subsection 4(c)(8) stating that "[t]he prohibitions in this section shall not apply . . ." makes clear that it only establishes exceptions to the general prohibitions of section 4(a). Moreover, section 4(c)(8) does not affirmatively extend the Board's jurisdiction to matters not already within the scope of section 4(a)(2). The express language of sections 4(a)(1) and 4(a)(2) forbids "*bank holding companies*"—not "banks"—from engaging in specified activities.

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[16] From the title of section 4—"INTERESTS IN NONBANKING ORGANIZATIONS"—to its specific language, every applicable provision of the BHC Act makes clear that section 4 does not govern banks.

[17] *Board of Governors v. Investment Co. Inst.*, 450 U.S. 46, 59 n.25 (1981). *See Cameron Fin. Corp. v. Board of Governors*, 497 F.2d at 848. *See also Patagonia Corp. v. Board of Governors*, 517 F.2d 803, 810-11 n.10 (9th Cir. 1975).

[18] 12 U.S.C. § 1843(a).

Petitioners contend that because section 4(c)(8) uses the words "subsidiary" and "company" and those words are defined to include banks, the restrictions of section 4(c)(8) must apply to banks. However, by *expressly excluding banks* in section 4(a), Congress indicated its intent that the term "company" as used in section 4 does not include banks. Further, the definition of "subsidiary" in section 2 was the result of a 1966 amendment to the BHC Act. As such, it sheds no light on what was intended by the Act's original language.[19]

The legislative history of the BHC Act supports the Second Circuit's conclusion that section 4 does not reach the activities of banks owned by holding companies. In enacting the original BHC Act of 1956 Congress did not indicate that the Act was intended to affect the activities of holding company-owned banks, whose powers have traditionally been regulated by their chartering authorities. Representative Spence, the Chairman of the House Committee on Banking and Currency and the chief sponsor of the House bill, specifically noted that the bill would not affect the powers granted to state banks under state law.[20] Moreover, Federal Reserve Board Governor Robertson testified that entities that were "merely an arm of the bank itself" would not be subject to the nonbanking prohibitions of the BHC Act.[21]

The legislative history of the 1970 amendments to section 4(c)(8) further clarified that section 4 does not reach the activities of banks owned by holding companies.[22] Moreover, in enacting Title VI of the Garn-

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[19] *See* 12 U.S.C. §§ 1841(d) & (g), *as amended by* Act of July 1, 1966, Pub. L. No. 89-485, §§ 4-6, 80 Stat. 236-37.

[20] *1955 House Hearings, supra* note 15, at 553.

[21] *See id.* at 119.

[22] *See* H.R. Rep. No. 387, 91st Cong., 1st Sess. 15 (1969) (prevailing views of the majority).

St Germain Depository Institutions Act of 1982,[23] Congress did not amend section 4(a) of the Act. Yet, as previously explained, section 4(a) is the critical provision because it contains the only relevant nonbanking prohibitions.

The Board consistently has ruled that activities conducted by holding company-owned state-chartered banks in accordance with state law are excluded from section 4. For example, in 1964 the Board declared that "the laws of the State in which [a holding company-owned state] bank operates . . . govern the right of the bank to provide a particular service."[24] Petitioners overemphasize the importance of *Citicorp* (American State Bank), 71 Fed. Res. Bull. 789 (1985), the only case where the Board asserted jurisdiction over the direct operations of a holding company-owned bank. The Board did so, however, only to prevent the use of the bank as a "device" to "evade" the restrictions on insurance activities under section 4(c)(8). The Board's decision was based upon its authority to "prevent evasions" of the BHC Act under section 5(b).[25] The Board stressed that it was not deciding the general question of whether section 4 applies to the activities of holding company-owned banks.[26]

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[23] Act of Oct. 15, 1982, Pub. L. No. 97-320, § 601, 96 Stat. 1536 (amending 12 U.S.C. § 1843(c)(8)).

[24] 12 C.F.R. § 225.118(c) (adopted 1964; redesignated 1971). *See also NCNB Corp.*, 72 Fed. Res. Bull. 57, 58 (1986); *Citicorp*, 72 Fed. Res. Bull. 714, 716 (1986).

[25] 12 U.S.C. § 1844(b); *Citicorp*, 71 Fed. Res. Bull. at 790-91 & nn. 3-6. Indeed, subsequent to the Board's *Citicorp* order, this Court cautioned the Board that Section 5(b) "only permits the Board to police within the boundaries of the [BHC] Act; it does not permit the Board to expand its jurisdiction beyond [those] boundaries." *Board of Governors v. Dimension Fin. Corp.*, 474 U.S. 361, 373 n.6 (1986).

[26] 71 Fed. Res. Bull. at 791 & n.6. *See also NCNB Corp.*, 72 Fed. Res. Bull. at 58 & n.11.

CONCLUSION

There being no important issues of federal law to decide, the petition for a writ of certiorari to the United States Court of Appeals for the Second Circuit should be denied.[27]

Respectfully submitted,

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July 24, 1990

[27] The arguments set forth in this brief are supported by the Independent Bankers Association of America and the National Council of Savings Institutions.

APPENDICES

APPENDIX I

STATE AUTHORIZATION OF SELECTED EXPANDED ACTIVITIES FOR STATE-CHARTERED BANKS *

(March 1990)

Insurance Underwriting

Delaware [1]
North Carolina
South Carolina
South Dakota
Utah [1]

Insurance Brokerage

Alabama
California
Indiana [8]
Iowa [9]
Nebraska
New Jersey
North Carolina
Oregon
South Carolina
South Dakota
Wisconsin
Wyoming

Real Estate Equity Participation

Arizona
Arkansas
California
Colorado
Connecticut
Florida
Kentucky
Maine
Massachusetts
Missouri
Nevada
New Hampshire
New Jersey
North Carolina
Ohio
Rhode Island
South Dakota
Tennessee [2]
Utah
Virginia
Washington
West Virginia
Wisconsin [3]

Real Estate Development

Arizona
Arkansas
California
Colorado
Connecticut
Florida
Kentucky
Maine
Massachusetts
Michigan
Missouri
Nevada
New Hampshire
New Jersey
North Carolina
Ohio
Rhode Island
South Dakota
Utah
Virginia
Washington
West Virginia
Wisconsin [3]

Real Estate Brokerage

Iowa
Massachusetts
New Jersey
North Carolina
Oregon
Wisconsin

Securities Underwriting

Arizona
California [6]
Delaware
Florida
Indiana [5]
Iowa
Kansas [10]
Maine
Massachusetts
Michigan
Missouri [4]
Montana [7]
New Jersey
North Carolina
Pennsylvania [11]
Washington
West Virginia

Securities Brokerage

Arizona
Connecticut
Delaware
Florida
Georgia
Indiana [5]
Iowa
Kansas
Maine
Maryland
Michigan
Minnesota
Nebraska
New Jersey
New York
North Carolina
Ohio
Pennsylvania
Texas
Vermont
West Virginia

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* Expanded activities above those permitted national banks and bank holding companies under the Bank Holding Company Act.

[1] Grandfathered institutions.

[2] Banks not allowed to be active partners in real estate development.

[3] Wisconsin enacted expanded powers legislation 5.86. New legislation authorized the Commissioner of Banking to promulgate rules under which state banks may engage in activities that are authorized for other financial institutions doing business in the state.

[4] Underwrite mutual funds and may underwrite securities to the extent of the state legal loan limit.

[5] Underwrite municipal revenue bonds and market mutual funds and mortgage-backed securities.

[6] Underwrite mutual funds; law silent on other securities.

[7] Limited to bonds.

[8] Cannot broker life insurance, all other types permitted.

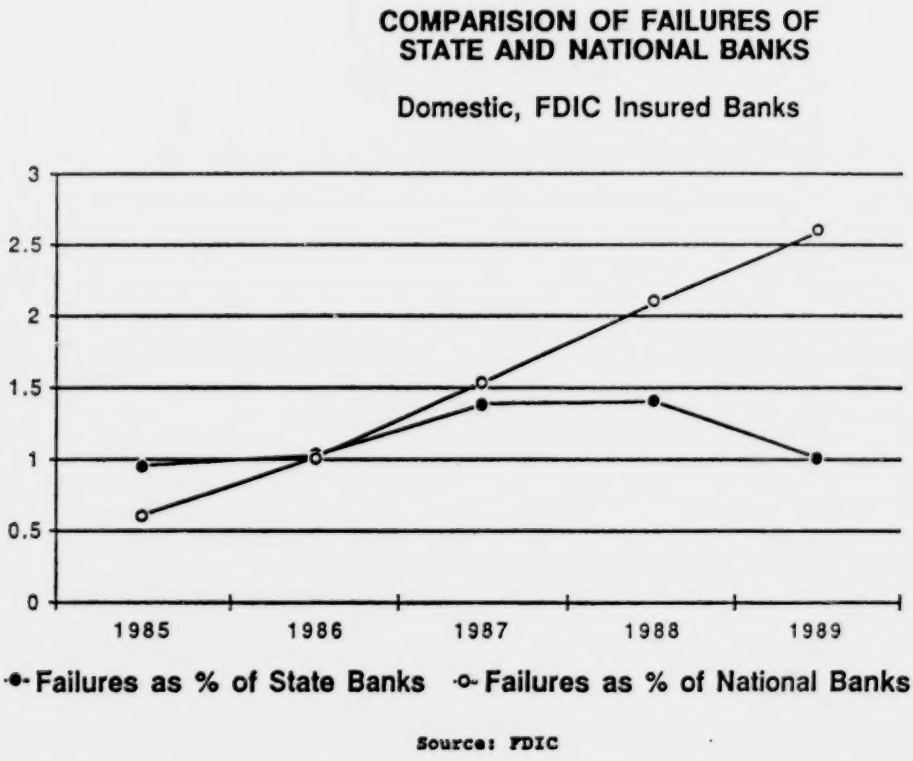
[9] Property and casualty only.

[10] Underwrite municipal bonds.

[11] Underwrite municipal and mortgage related securities to extent permitted savings banks.

Source: Conference of State Bank Supervisors, *State of the State Banking System* (1989).

APPENDIX II



Source: Conference of State Bank Supervisors, *State of the State Banking System* (1989).

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No. 89-1620

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, NEW YORK ASSOCIATION OF LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC. AND THE PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,

Petitioners,

v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,

Respondent,

MERCHANTS NATIONAL CORPORATION,

Intervenor.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit

BRIEF OF THE NATIONAL ASSOCIATION OF REALTORS® AS *AMICUS CURIAE* IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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BRIEF OF THE NATIONAL ASSOCIATION OF REALTORS® AS *AMICUS CURIAE* IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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* All parties of record in this case have consented to the filing of this brief *amicus curiae* in support of petitioners. These consents are filed herewith.

INTEREST OF THE *AMICUS CURIAE*

The NATIONAL ASSOCIATION OF REALTORS® (hereinafter "NAR") is the nation's largest trade association, comprised of over 800,000 persons engaged in all phases of the real estate business. Those members, who identify themselves by use of the federally registered collective membership mark "REALTOR® ", all subscribe to NAR's strict Code of Ethics and Standards of Practice.

The decision of the Second Circuit has widespread impact on the real estate industry. While the instant case involves the ability of banks to engage in insurance activities, its holding is in no way limited to insurance. The decision will also permit the banking industry to participate in all aspects of the real estate business, provided it is permitted by the chartering authority.

NAR opposes participation in the real estate business by financial entities which benefit from federal deposit insurance, favorable tax treatment, and special access to credit. The basis for this opposition is the likelihood that participation in real estate activities may conflict with the interests of their customers, threaten the safety and financial stability of the institution, increase the risk of taxpayer liability and pose a threat to the competitive structure of the real estate industry.

A determination of the circumstances under which a bank will be permitted to engage in nonbank activities, such as real estate, is of direct and immediate concern to the NAR and its membership.

ARGUMENT

The issue in this case is whether the nonbanking limitations of Section 4 of the Bank Holding Company Act (the "Act"), 12 U.S.C. 1843, apply to direct activities of bank subsidiaries of bank holding companies. The court of appeals accepted as reasonable the interpretation of the Board of Governors of the Federal Reserve System that vests national and state chartering authorities with the power to decide the permissible scope of nonbank activities of bank subsidiaries.

The result of this decision is that state bank subsidiaries of bank holding companies are not prohibited from engaging in any type of nonbanking activity permitted by state law, including all aspects of the real estate business, notwithstanding the fact that bank holding companies have been expressly forbidden from engaging in such activities by Section 4 of the Act.

Such a result, which permits subsidiaries to do precisely that which has been expressly forbidden to the parent is incongruous, eviscerates the Act and frustrates its very purpose.

NAR believes that the Board's construction of the Act is not only inconsistent with the plain dictates of common sense, but also incorrect as a matter of law. In that regard, NAR endorses and urges to the Court the legal arguments so ably presented by petitioners in their brief.

NAR also recognizes a pressing need for clarification of this issue by the Supreme Court at this time. Not only has this controversy been the subject of protracted litigation, it has also been the subject of periodic considera-

tion by the United States Congress. Clarification by the Supreme Court of the present status of the law will permit further debate of the issue in the Congress without the cloud of uncertainty that presently exists as to the correct reading of Congressional intent and legislative history.

CONCLUSION

For the foregoing reasons, NAR urges the Court to grant the petition for writ of certiorari.

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